Report
to
The LEGISLATIVE FINANCE COMMITTEE

Economic Development Department and Taxation and Revenue Department
Job Creation Incentives: The Job Training Incentive Program, the Local Economic Development Act, and Select Economic Development Tax Expenditures
August 23, 2012

Report #12-08

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August 23, 2012

Mr. Jon Barela, Secretary
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Ms. Demesia Padilla, Secretary
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Dear Secretaries Barela and Padilla:

On behalf of the Legislative Finance Committee (Committee), I am pleased to transmit the *Evaluation of Job Creation Incentives* for the Economic Development Department and the Taxation and Revenue Department. The evaluation team assessed the effectiveness of certain job creation tools including the Job Training Incentive Program (JTIP), Local Economic Development Act Grants (LEDA), and select economic development tax expenditures.

The report will be presented to the Committee on August 23, 2012. Discussions were held with each agency to address any concerns prior to the exit conference, which was conducted on August 15, 2012. The Committee would like a plan from the departments to address recommendations in this report within 30-days from the date of the hearing.

I believe this report addresses issues the committee asked us to review. We appreciate the cooperation and assistance from the agencies' staff.

Sincerely,

David Abbey, Director

Cc: Dr. Tom Clifford, Secretary, Department of Finance and Administration

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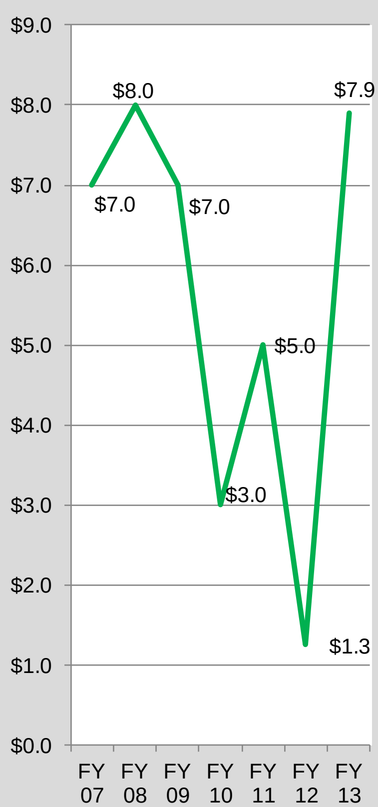
Significant Job Losses 2006-2012

Company	Year Closed	Jobs Lost
America Online	2006	900
Stream International	2008	500
Solo Cup	2008	200
Eclipse Aviation	2009	1,700
Convergys	2010	677
Proper Foods	2012	125
Schott Solar	2012	250

Source: NM Business Weekly, KRQE, ABQ Journal

JTIP Appropriations FY07-FY13
(In millions)



Source: EDD

With New Mexico's unemployment rate at 6.6 percent as of July 2012, creating quality sustainable job opportunities in the state is a primary concern. New Mexico is currently attempting to foster an environment conducive to economic growth through job creation with a combination of tax expenditures and direct incentives. Understanding the effectiveness of these different job creation strategies can assist the Legislature in proposing effective policies to promote quality employment growth.

This evaluation focuses on three programs designed to spur economic development in New Mexico: the Job Training Incentive Program (JTIP), the Local Economic Development Act (LEDA), which are both administered by the Economic Development Department (EDD), and a selection of tax credits administered by the Taxation and Revenue Department (TRD). In this evaluation, LFC reviewed five tax expenditures related to economic development: the High Wage Jobs Tax Credit, Rural Jobs Tax Credit, Investment Credit, Technology Jobs Tax Credit, and Research and Development Small Business Tax Credit.

Job creation incentives exist to attract businesses to the state and build the overall economy. In New Mexico, the JTIP subsidizes training costs for companies creating new jobs through expansion or relocation. LEDA provides capital for building infrastructure with the intent of creating new jobs. Tax expenditures reduce costs to companies by reducing their tax liability.

As a package, these incentives can make New Mexico more competitive as companies look at different states to locate. However, all three programs have weaknesses in accountability, reporting, and assessing program value. There is no comprehensive review or regular analysis of all job creation incentives to inform budget decisions. The state of New Mexico is unable to demonstrate the return taxpayers are receiving on their dollars.

Various issues complicate managing economic development incentives in New Mexico including statutorily required confidentiality around tax data, LEDA agreements without clawbacks to recoup state funds, and a lack of consistent reporting requirements for program participants to measure effectiveness. Other states have addressed these issues by requiring public disclosure of taxpayer data for those receiving economic development tax credits, only reimbursing companies through grant programs based on actual jobs created instead of the intent of job creation, and creating parameters for measuring total investments across direct incentive programs and indirect incentives through tax credits. These steps create transparency, accountability and a manner to measure how the entire system of incentives work together in creating jobs.

New Mexico uses a combination of tax expenditures and direct incentives to promote job creation.

There is no comprehensive and regular analysis by executive agencies charged with administering economic development incentive programs.

KEY FINDINGS

New Mexico lacks a comprehensive approach for financing and monitoring performance of job creation incentives. The state uses a mix of incentives for job creation that cost an estimated $467.5 million between FY07 and FY11, including tax expenditures, direct incentives such as the JTIP, and capital infrastructure investment though LEDA. The vast majority of the state's investment in economic development occurs within the tax code through various tax credits, totaling foregone revenue of $374.5 million, followed by grants through LEDA totaling $63 million. The state spends the least on direct incentives under the JTIP, with a total of $30 million expended between FY07 and FY11.

Previous LFC analyses highlighted a fragmented and uncoordinated approach to job creation, which continues to this day. In a 2009 LFC brief, staff identified various areas of concern in the execution and monitoring of economic development incentive programs and offered the following recommendations:

1. Prepare a statewide economic development plan that includes a variety of high-performance measures;
2. Require incentive agreements;
3. Link incentives to performance;
4. Establish minimum wage standards for job creation and retention requirements; and
5. Require incentive recapture (clawbacks) for non-performance.

Lack of a comprehensive and regularly produced tax expenditure budget hampers decision-making and monitoring foregone revenue costs to the state. The Taxation and Revenue Department (TRD) was due to release a Tax Expenditure Report in summer 2012 per executive order, but as of the publishing of this evaluation, the report has not been released publicly. The Tax Expenditure Report is a first step in reviewing the effectiveness of tax credits for achieving policy goals. The TRD's testimony at the LFC July 2012 hearings indicates it is a tool for identifying and referencing the large amount of tax expenditures in statute. Further steps are needed to bring New Mexico in line with best practices of in-depth analysis.

The Pew Center for the States released a report in 2012 describing various methods for measuring tax incentive effectiveness:

1. *Build evaluation of incentives into policy and budget deliberations.*
2. *Establish a strategic and ongoing schedule to review tax expenditures.*
3. *Ask and answer the right questions using good data and analysis.*
4. *Determine whether tax incentives are achieving the state's goals.*

The report rated New Mexico as having mixed results in its ability to effectively review its tax credits, exemptions and deductions.

Without across-the-board strategic planning and accountability, the state is not well-positioned to invest in incentives that create jobs at a reasonable cost to taxpayers. Total incentives given to a particular company, including tax credits, are valuable information for the Legislature and taxpayers. In the case of Schott Solar, for example, the company received state and city LEDA grants, JTIP reimbursements, loans facilitated through the New Mexico Finance Authority, and likely also received High Wage Job Tax credits. Due to lack of communication and coordination between the various entities supporting Schott Solar, it is difficult to accurately value the costs and benefits of these incentives and losses from the plant's closure.

Within a sample of incentive recipients, 96 percent of state investment in economic development occurred through the tax code.

Information sensitivity and issues of confidentiality have proven a significant barrier in performing a thorough assessment of economic development programs. State law requires the TRD to maintain taxpayer confidentiality. This has presented a problem in performing a thorough assessment of tax incentives, even leading to data being omitted by the department in their reporting to omit identifying information. LFC staff does not have access to confidential data, and therefore cannot perform an in-depth study of the effectiveness of tax credits. The JTIP would be able to more effectively measure success of the program if it could monitor a trainee's progress through unemployment insurance filings housed at the Workforce Solutions Department (WSD).

The Economic Development Department reports the number of jobs created based on company reports of anticipated jobs, not actual jobs created.

Combined incentives cost an estimated $31 thousand for each job subsidized by the state, but the EDD and the TRD do not analyze or report this total cost per job created. Based on cost per job analysis on a sample of companies receiving incentives, it costs the state of New Mexico on average an estimated $31 thousand to attract a job, with an average salary of $43 thousand. The LFC performed this analysis based on JTIP and LEDA funding data and independently estimated sample companies' eligibility for the High Wage Jobs Tax Credit and the Rural Jobs Tax Credit for companies awarded JTIP funds between FY07 and FY11. While many states review economic development programs or tax expenditures, LFC staff did not find evidence of another state analyzing combined cost of tax credits and direct incentive programs on job creation. The TRD and the EDD do not currently analyze costs to the state of all job creation incentives per job they create. Furthermore, the TRD does not report a number for jobs created from a particular tax credit, making an actual versus estimated total cost per job with tax incentives for all jobs created difficult to assess.

Other states' best practices suggest ways to quantify the effectiveness of incentives for economic development in light of greater economic factors the state does not control and provide better accountability over jobs created. In an independent analysis of Kentucky's economic development incentives, it calculated a cost per job to the state based on direct incentives, tax credits, and costs to run their version of the EDD.

In Minnesota, statute requires taxpayer data related to specific tax credits be made public.

In 2012, Hawaii completed a legislative audit of its high-technology business and research activities tax credits and found for a program costing almost $1 billion in foregone revenue, the state cannot measure or assess the credit's effectiveness. The audit concluded the state is unable measure the impacts of credits in order to justify losing an amount of revenue this size without legislative oversight.

North Carolina has two main highly-competitive, performance-based discretionary incentive programs, where state funds are only disbursed for actual jobs created. In addition, North Carolina's recent economic development inventory is a step toward providing the tools needed to encourage better legislative and executive oversight of economic development spending.

Since 2007, the state has issued $64 million in Local Economic Development Act grants without safeguards to ensure jobs are created. From 2007 to 2011, the EDD has received $64 million in capital outlay appropriations to provide LEDA grants statewide. The grants were distributed to various political subdivisions and for specific economic development projects such as Schott Solar and Fidelity Investments in Bernalillo County. As of June 2012, 29 LEDA projects total $56 million, of which 19 are complete.

The state could have recovered an estimated $5.5 million from Schott Solar if a similar clawback as the city of Albuquerque's was in place for state funds.

LEDA agreements do not include clawback provisions, keeping the state from recouping any funds if a company closes or reduces its workforce. Clawbacks are limited to the local entity's contributions and not state funds, even when the state has contributed a larger portion of the funding. In 2009, the LFC reported that state incentive agreements need to link incentives to performance and recommended the state require incentive clawbacks for non-performance.

Job creation requirements vary and there are no requirements in place for job retention. The 2009 LFC Brief on the Survey of Economic Development Initiatives recommended that minimum standards for both job creation and retention be established. Hewlett Packard's project participation agreement (PPA) with the city of Rio Rancho clearly defines the number of jobs with a full-time-equivalent as 2,080 hours per year. Examples of the various job creation requirements in other project participation agreements include:

The EDD does not always require municipalities to report job creation numbers.

- Job creation defined in job years and it is not always clear how many jobs are to be created;
- Target number of jobs created on an annual basis with and without a cumulative total; and
- Direct or indirect number of hours within a stipulated time period or over a period of time, not specific as to number of jobs to be created.

Having different job creation requirements makes it difficult to capture benchmark data. In some instances, there are targets in the PPAs for maintaining a certain number of jobs over time, but none of the nine PPAs the LFC reviewed include specific requirements for job retention.

Better accountability measures are needed to ensure the Job Training Incentive Program produces sustainable long-term results. In FY11, the program paid out $1.2 million to support the creation of 613 jobs, 43 of which were in rural areas. Average trainee salary for FY11 totaled $58 thousand per year.

Originally created to expand employment in manufacturing, the JTIP now primarily funds call center jobs.

JTIP has a clawback provision, but EDD has never clawed back funds since the provision was introduced in 2007.

TRD has not met the statutory requirements for reporting to the Legislature on the Investment Credit, Technology Jobs Credit, and Rural Jobs Credit.

The High Wage Job Tax Credit has grown from $9.3 million to $48.1 million, or 520 percent between FY11 and FY12, at a time of minimal job growth.

JTIP funds small and large projects alike without a prioritization that aligns with an overall state economic development strategy. Funds are currently made available on a first-come-first-served basis instead of being budgeted strategically to achieve specific goals. In the EDD FY13 strategic plan, the JTIP's objectives include increasing company participation in the program, increasing the number of jobs funded, and sustaining the quality of jobs funded. The plan reflects the focus on total jobs trained as opposed to having a strategic focus for different industries in different areas of the state based on region-specific strengths.

The JTIP paid $25 million in reimbursements of a total $50.2 million, or 50 percent encumbered between FY07 and FY11. Job and wage data provided in the JTIP application have been amended during the contract period. These amendments account for actual reimbursement payments being less than originally budgeted. While unexpended funds are eventually unencumbered and returned to the overall JTIP budget, this 50 percent differential in budgeting may prevent other applicants from being able to access funds.

JTIP performance measures do not meaningfully assess the effectiveness of the program. If JTIP is a job creation incentive, performance measures currently in place do not measure effectiveness through job retention or changes in employee wages at the recipient company. However, if JTIP is intended as a workforce training program, then performance measures should be tied to the trainee over the long-term.

The Taxation and Revenue Department cannot accurately measure foregone revenue or impact from tax expenditures designed to spur economic growth. The TRD does not routinely review and report effectiveness of economic development tax credits to the Legislature, which is inconsistent with best practices, and in some cases, does not comply with statute. For example, for the Rural Jobs Tax Credit, the WSD and the EDD are required to evaluate and report on the credit in conjunction with the TRD, but none of the three agencies could produce a report for this credit that had been presented to the Legislature.

The state does not have an established regular timeline for evaluating tax expenditures. While some credits do have requirements for review within statute, this does not span all credits. Similarly, while some credits such as the High Wage Jobs Tax Credit have sunsets, New Mexico does not have universal sunset provisions for tax expenditures. Evaluation timelines and sunset provisions both create a timely process for reviewing tax expenditures.

The TRD does not have a system for collection and analysis of tax expenditure data, limiting its ability to measure effectiveness and inform the Legislature. In the case of the economic development tax expenditures reviewed for this evaluation, TRD does not have a method for cataloguing data and performing analysis electronically. Tax forms provide a great deal of data that could be used to measure how the tax credits perform. However, LFC staff does not have statutory authority to access the data needed to assess the effectiveness of these expenditures.

The High Wage Jobs Credit's recent increase makes it comparable in size to the Film Production Credit, raising similar concerns over future unchecked growth. Constituents have voiced their concerns in other interim committees over potential loopholes in the language of the High Wage Job Credit statue, creating potential gray areas in claiming and administering the credit. In testimony before the Revenue Stabilization and Tax Policy Committee, Albuquerque Economic Development (AED) identified four areas to be addressed:

- *Definition of Wages to Determine Size of Credit*
- *Wage Rates*
- *Lack of Time Limits to Claim Credit*
- *Sunset Provision*

The AED also testified that during this interim, representatives from the EDD, the TRD, the Department of Finance and Administration, and the economic development community are convening to draft legislation to address some statutory issues surrounding the High Wage Jobs Tax Credit.

KEY RECOMMENDATIONS

The Legislature should formalize within statute

- Public disclosure requirements for businesses receiving economic development tax credits;
- Clawback provisions for all economic development direct expenditures to ensure clawback requirements are consistently applied.
- Prioritizing cost-effective evidence based economic development incentives;
- Sunset provisions for economic development tax incentives, including regular review of fixed wage and population definitions for credit eligibility; and
- Guidelines for reporting on all tax credits to the Legislature to create uniformity in information being reported and frequency of reporting.

The Economic Development Department should

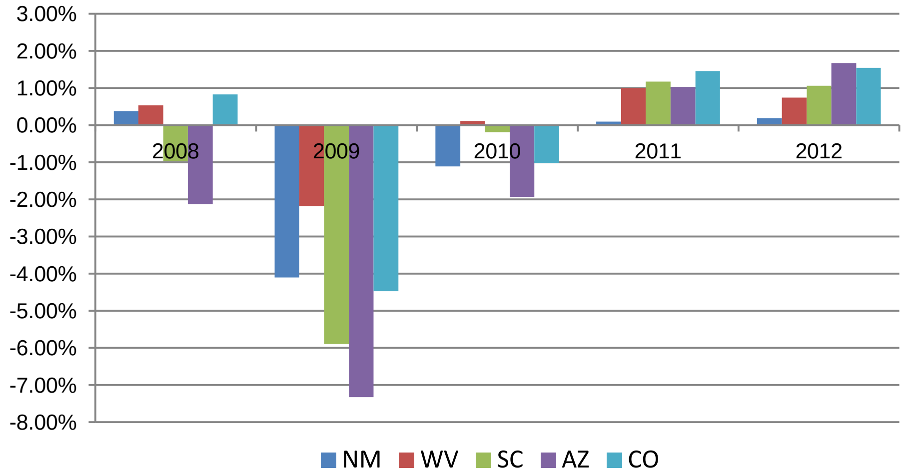
- Include clawback provisions for state funds in its intergovernmental agreements, and require local entities to include clawback provisions for state funds in its project participation agreements;
- Establish a standard requirement for defining the number of jobs created;
- Include job reporting requirements in the intergovernmental agreements for the LEDA that include actual jobs created and retained, holding the local entity responsible for obtaining the information and providing the quarterly wage and contribution reports to the state to ensure accountability through the duration of the company's project participation agreement;
- Institute state-specific minimum wage and job count requirements to fully access JTIP reimbursement to drive economic development goals for the state; and
- Require JTIP recipient companies to report on job retention and wages for a period of time after final reimbursement for longitudinal analysis, such as three to five years.

The Taxation and Revenue Department should

- Research and formalize a measure of economic return to the state from job growth in conjunction with economic research resources such as the Bureau for Business and Economic Research at the University of New Mexico (BBER) or the Arrowhead Center at New Mexico State University;
- Follow current statutory requirements on the reporting of economic development tax expenditures; and
- Establish criteria for tax expenditure analysis using recommendations from the Pew Center for the States as a guide.

Between 2008 and July 2012, New Mexico's employment shrunk an average of 4.5 percent. While the state did not encounter the same employment declines as other states such as Arizona and South Carolina, New Mexico has not fully recovered from job losses, with employment gains in the first half of 2012 at 0.2 percent.

New Mexico Non-Farm Employment Growth 2008-2012



Source: U.S. Bureau of Labor Statistics

Economic Development Department (EDD). The EDD was created pursuant to the Economic Development Act in Sections 9-15-1 through 9-15-55 NMSA 1978. The EDD's mission is to enhance and leverage a competitive environment to create jobs, develop the tax base and provide incentives for business development. The department promotes economic development and diversification, as well as business recruitment, expansion, and retention in New Mexico. The EDD provides a coordinated statewide perspective on economic development activities, maintains a database for local and regional economic development groups, and serves as the comprehensive source of information for businesses wishing to locate or expand in the state.

Table 1. Economic Development Department Budget Summary
($ in millions)

Fiscal Year	Budget Actual	% Change	Authorized FTE
2007	$7,318.0		67
2008	$9,382.0	28%	68
2009	$9,750.8	4%	70
2010	$9,209.5	-6%	65
2011	$7,728.3	-16%	65

Source: LFC Vol. II

Job Training Incentive Program. The Job Training Incentive Program (JTIP) supports economic development in New Mexico by reimbursing qualified companies for a significant portion of training costs associated with newly created jobs. The JTIP program, previously known as the Industrial Training Development Program (Section 21-9-7 NMSA 1978) strengthens New Mexico's economy by providing financial incentives to companies that create new economic-based jobs in New Mexico.

The JTIP reimburses qualified companies for a portion of training costs associated with job creation. The program provides for classroom or on-the-job training, reimbursing an expanding or relocating business for up to 75 percent of a trainee's wages for up to six months. The amount of the award depends on the number and complexity of jobs, the wages paid, and the business location.

To qualify, new or expanding companies must either create a product in New Mexico, or provide a non-retail service with 50 percent of the company's customer and revenue base outside of the state. The eligible jobs must be full-time and year-round. The trainee must be a new hire to the company, must be a current New Mexico resident, and have resided in the state for at least one continuous year at any time prior to being hired.

Local Economic Development Act. The Local Economic Development Act (LEDA), Section 5-10-1 NMSA 1978, allows communities to provide assistance to qualified economic development projects while maintaining safeguards against the unauthorized use of public resources.

Economic development projects must create new job opportunities. After a local governmental entity creates and adopts an economic development plan, a qualifying business is required to submit a project application, including all information the local government deems necessary. Projects are approved by ordinance, and the local government may negotiate with a qualifying business on the type and amount of assistance to be provided. In order to qualify for Economic Development Capital Outlay funds, the following must be completed:

- An endorsed copy of the initial ordinance adopting a Local Economic Development Act;
- A description of how the funds will be used (scope of work) along with appropriate documentation (purchase of land, loan approval, infrastructure order, etc.);
- A copy of the project application;
- A copy of the project participation agreement;
- The local government needs to adopt the project by ordinance attaching the application, project participation agreement and proof of notice to the public; and
- A letter by the local government requesting the monies be transferred, a description of the due diligence performed (cost-benefit and financial analysis), and a statement the project complies with LEDA.

Since 2002, sixty-four New Mexico communities have passed a Local Economic Development Act. Through passing LEDA, a community adopts an ordinance creating an economic development organization and a strategic plan. This empowers communities to embark on economic development projects tailored to their needs.

Taxation and Revenue Department (TRD). The TRD administers tax credit programs. Tax expenditures are a method to advance policy through the tax code by incentivizing taxpayer behavior. In the case of economic development, this mostly takes the form of tax credits applied against a taxpayer's total tax liability to the state. Tax expenditures are a form of spending, as they reduce the amount of revenue going into the state's general fund, allowing the taxpayer to keep more of their income. This comes in exchange for promoting a particular behavior, such as increasing job growth in rural areas, fostering a particular industry such as film, or increasing wages paid by employers operating in New Mexico. Furthermore, tax expenditures are a method of increasing a state's competitive advantage in recruiting businesses.

In a January 2012 report, Ernst and Young compared New Mexico's tax rate for industries to a select group of western states for a hypothetical manufacturer. Before tax credits, New Mexico's effective tax rate was 15.9 percent, compared to the other states' average effective tax rate of 7.3 percent. However, after applying available tax credits, New Mexico's effective tax rate drops to 6 percent, making it the third lowest rate among the sample set of states. This study demonstrated the role tax credits play for New Mexico in competing with other states to attract new businesses.

Table 2. State Effective Tax Rates Ranked

State	Before Tax Credits Effective Tax Rate	Before Tax Credits Rank	After Tax Credits Effective Tax Rate	After Tax Credits Rank
Arizona	8.4%	4	6.5%	5
California	7.9%	5	7.6%	3
Colorado	6.6%	7	6.5%	4
Nevada	6.9%	6	6.0%	7
New Mexico	15.9%	1	6.0%	6
Oklahoma	10.8%	2	10.3%	1
Oregon	2.4%	9	2.2%	9
Texas	9.5%	3	9.5%	2
Utah	5.6%	8	5.3%	8
Other States' Average	7.3%		6.7%	

Source: NM Tax Research Institute Business Tax Competitiveness Study

The LFC identified nine tax expenditures related to economic development spanning across personal and corporate income tax, gross receipts tax, and property tax among others, totaling approximately $9 million in foregone revenue for FY11. The largest tax credit is the Film Production Credit at $76.2 million, followed by the High Wage Jobs Tax Credit at $10.4 million. No other credit in this category surpasses $4 million; however they range across a variety of areas including technology and investment, rural jobs, and research and development. The table below lists tax credits related to economic development, but not all of these credits have a job creation requirement.

Table 3. Foregone Revenue for Economic Development Tax Expenditures
(in thousands)

Title	FY2007	FY2008	FY2009	FY2010	FY2011	Total
Film Production Credit	$17,873.7	$46,217.0	$76,922.4	$69,310.9	$76,252.5	$286,576.5
Laboratory Small Business Credit	N/A	$0.0	$2,525.3	$2,394.2	$3,188.0	$8,107.5
Tax Increment Districts	N/A	N/A	$2,946.1	$1,370.9	$3,810.8	$8,127.8
Angel Investment Credit	$0.0	$145.0	$157.8	$200.8	$80.8	$584.4
Investment Credit	N/A	$806.8	$9,033.6	$7,037.9	$1,862.9	$18,741.2
Technology Jobs Credit	$59.9	$1,909.8	$5,916.4	$6,265.3	$3,112.7	$17,264.1
High Wage Jobs Tax Credit	$1,262.6	$2,582.5	$14,438.0	$4,579.7	$10,402.3	$33,265.1
Rural Jobs Tax Credit	N/A	$179.5	$422.7	$664.6	$295.5	$1,562.3
R&D Small Business Tax Credit	N/A	$133.1	$107.1	$0.5	N/A	$240.7

Source: TRD

NEW MEXICO LACKS A COMPREHENSIVE APPROACH FOR FINANCING AND MONITORING PERFORMANCE OF JOB CREATION INCENTIVES

The state uses a mix of incentives for job creation that cost an estimated $467.5 million between FY07 and FY11, including tax expenditures, direct incentives such as the JTIP, and capital infrastructure investment though LEDA. The vast majority of the state's investment in economic development occurs within the tax code through various tax credits, totaling estimated foregone revenue of $374.5 million, followed by grants through LEDA totaling $63 million. The state spends the least on direct incentives under the JTIP, with a total of $30 million expended between FY07 and FY11.

Previous LFC analyses highlighted a fragmented and uncoordinated approach to job creation, which continues to this day. In a 2009 LFC brief, staff identified various areas of concern in the execution and monitoring of economic development incentive programs including inconsistent or incomplete data, programs fragmented between agencies, a lack of a statewide economic development plan, and clawback provisions for noncompliance. As part of this analysis, the LFC staff made five recommendations to improve effectiveness and accountability in economic development programs:

1. Prepare a statewide economic development plan that includes a variety of high-performance measures;
2. Require incentive agreements;
3. Link incentives to performance;
4. Establish minimum wage standards for job creation and retention requirements; and
5. Require incentive recapture (clawbacks) for non-performance.

While the Economic Development Department (EDD) has implemented portions of these recommendations, the majority of them have not been addressed, leading to programs being utilized as subsidies instead of performance-driving incentives, as well as no recourse for the state to recover funds, causing losses to the state totaling tens of millions of dollars.

Lack of a comprehensive and regularly produced tax expenditure budget hampers decision-making and monitoring foregone revenue costs to the state. The Taxation and Revenue Department (TRD) was due to release a Tax Expenditure Report in summer 2012 per executive order, but as of the publishing of this evaluation, the report has not been released publicly. The Tax Expenditure Report is a first step in reviewing the effectiveness of tax credits for achieving policy goals. The TRD's testimony at the LFC July 2012 hearings indicates it is a tool for identifying and referencing the large amount of tax expenditures in statute. Further steps are needed to bring New Mexico in line with best practices identified in other states.

The Pew Center for the States released a report in 2012 describing various methods for measuring tax incentive effectiveness. The report rated New Mexico as having mixed results in its ability to effectively review its various tax credits, exemptions, and deductions. While the report recognized that the state does look at economic impact, the TRD does not have a mechanism to inform policy decisions, report on all tax incentives, or draw clear conclusions on how the largest economic development program in the state is performing.

The Pew report identified various ways states can improve their analysis of tax incentives to better inform policymakers:

1) *Build evaluation of incentives into policy and budget deliberations.* States do not generally include a review of tax expenditures in budget discussions. However, tax incentives are a form of spending, as they reduce revenues flowing into a state's general fund. Therefore, to have a complete picture of a state's cash inflows and outflows, a regular review of tax expenditures is essential. Arizona, Iowa, Oregon, and

Washington currently integrate tax expenditure analysis into their policymaking process. In Washington, members of the state's nonpartisan Joint Legislative Audit and Review Committee staff review a tax incentive's performance to its objective and offers recommendations on whether to continue, modify, or terminate the incentive. The report is presented to a citizen commission and to legislative fiscal committees.

2) *Establish a strategic and ongoing schedule to review tax expenditures.* States have various schedules for reviewing tax incentives varying from annually to revolving schedules ranging from five to ten years. Different timelines and depth of review have tradeoffs regarding resources required to complete analysis, so states have to decide how frequently and how in depth a review of tax incentives should go. For example, Connecticut performed a review in 2010 that analyzed the effect of tax credits dating back to 1995, allowing a thorough historical economic impact analysis. Going forward, tax credits would be reviewed every three years.

3) *Ask and answer the right questions using good data and analysis.* The Pew Center identified various questions that any analysis of tax expenditures should consider:

    a. *Cause and Effect:* To what extent did the incentive reward a certain business decision, and how much did the incentive reward behavior that would have occurred in spite of the incentive?
    b. *Winners and Losers:* To what extent does the incentive benefit some at the expense of others?
    c. *Unintended Beneficiaries:* Do benefits of the incentive go beyond state borders?
    d. *Timing:* When will the costs of the incentive occur, and how long will they last?
    e. *Economics of Budget Trade-Offs:* What were the adverse economic effects of the incentive, and do the benefits of the incentive outweigh this negative impact?
    f. *Indirect Impacts:* To what extent do the investments of businesses receiving incentives filter into the broader economy, causing positive economic gains?

4) *Determine whether tax incentives are achieving the state's goals.* The greatest challenge in measuring tax expenditure effectiveness is having a clear and measurable goal. All tax incentives have the goal of creating some sort of economic impact, but being able to pinpoint whether that impact is to ease restrictions for investment or to create jobs in rural areas helps to frame specific impact analysis.

These guidelines suggest areas where the state can improve its analysis of tax expenditures. Currently, foregone revenue related to tax incentives is part of revenue analysis, but is not a part of the budgetary process. Performing a cost benefit analysis of tax expenditures, and whether they are achieving more than what the same revenue could achieve within a state program could prove useful in making budgetary decisions.

There is no comprehensive and regular analysis by executive agencies charged with administering economic development incentive programs. While the TRD and the EDD often report on the status of economic development incentives to the Legislature, they do not regularly analyze how effective these incentives are as a total package. Various tax credits such the High Wage Jobs Tax Credit and the Rural Job Tax Credit require coordination between the EDD and the TRD on areas such as certification of eligible taxpayers and reporting to Legislative committees. However, this appears to be a separation of tasks, and not a true collaboration. For example, taxpayers wishing to take advantage of the Rural Jobs Tax Credit must also be participating in JTIP. The EDD staff will provide the TRD with lists of rural JTIP recipients, but that is the extent of their involvement with the credit.

Without across-the-board strategic planning and accountability, the state is not well-positioned to invest in incentives that create jobs at a reasonable cost to taxpayers. Total incentives given to a particular company, including tax credits, are valuable information for the Legislature and taxpayers. In the case of Schott Solar, for example, the company received state and city LEDA grants, JTIP reimbursements, loans facilitated through the New Mexico Finance Authority, and likely also received High Wage Job Tax credits. Due to lack of communication and coordination between the various entities supporting Schott Solar, it is difficult to accurately value the total loss to the state when the company closes its plant in 2012. Schott Solar received over $20 million in direct public funding or through loans facilitated by public entities. This number is higher when considering tax credits claimed, but this data is not available to the LFC. As long as the state continues to offer various incentive programs managed through various state agencies, it will be important to establish a uniform reporting mechanism to get an accurate picture of how the state is investing taxpayer dollars in economic development.

Information sensitivity and issues of confidentiality have proven a significant barrier in performing a thorough assessment of economic development programs. State law requires TRD to maintain taxpayer confidentiality. This has presented a problem in performing a thorough assessment of tax incentives, even leading to data being omitted by the department in their tax expenditure reporting to omit identifying information.

The staff of Washington's Joint Legislative Audit and Review Committee has data sharing agreements in place with their revenue agency to provide taxpayer-level detail on credits claimed to integrate into their review of tax incentives. This provides a strong foundation to analyze and draw conclusions on which taxpayers are attracted to which credits, and whether this matches the original intent of the incentive. The LFC staff does not have similar access to confidential data, and therefore cannot perform an in-depth study of the effectiveness of tax credits.

The JTIP would be able to more effectively measure success of the program if it could monitor a trainee's progress in areas such as earning potential over their professional lifetime. This data is reported to the Workforce Solutions Department (WSD) as part of unemployment insurance filings. These same filings would provide the EDD an accurate job count so the agency would not have to rely on press releases and company self-reporting to calculate job creation. The EDD did collaborate with the WSD to track wages of JTIP trainees for the period of 2002-2004, but has not performed this type of analysis since. The results were included in a marketing brochure for the program. The EDD analysis showed that trainee wages increased on average 37 percent in the year immediately following JTIP participation when compared to the year prior. It is clear that having access to information housed across agencies could be vital in performing a thorough analysis of economic development programs. However, confidential employee information housed at the WSD has made accessing valuable employee data challenging.

The Economic Development Department reports the number of jobs created based on company reports of anticipated jobs, not actual jobs created. The reported number of jobs created is misleading. Because the data is based on projected jobs, the number of jobs created is not reduced by the number of jobs lost or abandoned over the same period. This also leaves a gap for reporting job retention and does not reflect outcomes. Tracking projected jobs created compared to actual jobs created would be valuable and could be used to demonstrate the success of individual projects and the department's programs as a whole. Job counts reported in the table below are self-reported projections by companies, not actual jobs created.

Table 4. New Mexico Economic Development Department
Summary of Job Creation Performance Measures

Description	2008	2009	2010	2011	2012 3rd Qtr
Annual net increase in jobs created due to economic development department efforts	5,582	4,570	2,763	1,922	2,212
Total number of rural jobs created	1,890	1,641	1,446	958	1,330
Number of jobs created through business relocations facilitated by the economic development partnership	3,984	2,225	767	499	577

Source: LFC Performance Report Cards

Without the proper data to measure outcomes for job creation and job retention, the department cannot effectively measure performance and benchmark its programs. The EDD's performance measure process needs improvement. For those programs that are intended to create jobs and retain existing employees, agencies could complement their measures by tracking and reporting additional information, such as the average wages of the jobs created and whether they offer benefits such as health care or paid time off. The EDD does not include requirements in its intergovernmental agreements with the local governments and JTIP contracts for providing quarterly job wage and contribution reports submitted to the Workforce Solutions Department as part of the company's responsibilities. It is not sufficient for the department simply to require reporting, it must take steps to ensure the reported outcomes are accurate and monitored.

The EDD performance monitoring plan in the Performance Based Budgeting System (PBBS) is incomplete. Although the department has a performance measure monitoring plan as required by the Accountability in Government Act (AGA), Section 6-3A-8D NMSA 1978, when the LFC inquired, the EDD staff was unaware it existed. The monitoring plan does not always include specifically where the information comes from, how it is collected, and a clear and specific description of how the measure is calculated. For example, the data source for the number of workers trained by the JTIP described the program and application process but did not include tracking the actual number of trained individuals. In addition, some measures do not include the required elements of a monitoring plan, such as the measure definition, data sources and the method in which the measure is calculated. The lack of input, processing, and review controls indicates that the Economic Development Department performance measure data may not be reliable.

Combined incentives cost an estimated $31 thousand for each job subsidized by the state, but the EDD and the TRD do not analyze or report this total cost per job created. Based on cost per job analysis on a sample of companies receiving incentives, it costs the state of New Mexico on average an estimated $31 thousand to attract a job, with an average salary of $43 thousand. This total includes JTIP, LEDA when applicable, and estimated foregone revenue from the High Wage Jobs Tax Credit and the Rural Jobs Tax Credit for a sample of companies awarded JTIP funds between FY07 and FY11. The LFC performed this analysis based on JTIP and LEDA funding data and independently estimated sample companies' eligibility for the selected tax credits **(Appendix B - Sample Cost per Job Analysis)**. While many states review economic development programs or tax expenditures, LFC staff found only one example of a state attempting to analyze combined cost of tax credits and direct incentive programs on job creation. Being able to assess total combined cost to the state per job created would allow policymakers to prioritize the most cost-effective incentives.

In 2010, per capita income was $40 thousand for New Mexico, and $47 thousand for the entire United States, according to the Bureau for Business and Economic Research (BBER) at the University of New Mexico. Based on this sample, it appears economic development programs are successful in creating jobs that pay an annual salary 7 percent higher than average, yet the cost to do so is high, as the state invests 72 cents for every dollar of wages for the first year of a newly created job.

Furthermore, within the sample set, 96 percent of state investment in economic development occurs through the tax code without any way of measuring how effective these dollars are in producing sustainable economic base jobs in New Mexico. The TRD does not report a number for jobs created due to a particular tax credit, making a total cost per job with tax incentives for all jobs created difficult to assess. Therefore, the state cannot pinpoint the total cost of a job created.

A complete return on investment analysis for economic development programs has never been completed and proves to be a complex task. The cost per job calculation is a standard formula of cost divided by jobs used to calculate effectiveness for economic development incentives. The EDD is required to report on cost per job performance measures, but the TRD is not. Furthermore, cost per job does not address the question of total economic impact of new jobs being created. The LFC staff attempted to quantify a return on investment to the state through tax revenue, but without access to data specific to taxpayers claiming economic development tax credits, even a basic analysis of this nature would not be useful. The Virginia Economic Development Partnership attempted to quantify the benefits of economic development incentives looking at both return on investment (ROI) and input-output models. The partnership's conclusion was the ROI model did not include all costs to the state providing services to the firm, its employees and other associated economic activities. The input-output model assumed all suppliers and existing firms (inputs) to the new business (output) would be positively impacted by the business moving in, but both inputs could be negatively impacted. Due to the many considerations required to accurately assess economic benefit, results can vary, as shown in studies completed on the impact of the film industry in New Mexico.

Other states' best practices suggest ways to quantify the effectiveness of incentives for economic development in light of greater economic factors the state does not control, and provide better accountability over jobs created. In a report commissioned by the Kentucky Legislature in 2012, an independent consulting firm recommended state agencies managing economic development incentive programs produce an annual comprehensive report of all incentives, both direct and indirect. The consultant noted this would require collaboration between two separate state agencies on monitoring and reporting standards. The report goes on to state that analysis should include summary measures such as jobs created or retained, investments made by programs, foregone revenue from tax credits or grant programs, and number of new projects approved. This type of collaborative analysis is not occurring in New Mexico between the EDD and the TRD.

In Kentucky's analysis of its economic development incentives, the consulting group estimated a cost per job to the state based on direct incentives, tax credits, and costs to run their version of the EDD. Over the ten-year period of 2001-2010, the average gross cost per job was $3,330. For comparison, Kentucky had a population of 4.4 million and per capita income of $23 thousand in 2010 according to the U.S. Census.

Table 5. Kentucky Calculation for Cost per Job

Add:
Total Foregone Revenue from Economic Development Tax Credits
Total JTIP Dollars Paid Out
Total LEDA Dollars Awarded
EDD Total Budget Appropriation
Total:
Total Jobs Created by Economic Development Activities
Average Annual Cost per Job

Source: Anderson Economic Group Review of Kentucky Economic Development Incentives

In Minnesota, statute requires taxpayer data related to specific tax credits be made public. The Small Business Investment tax credit program requires an annual report be published to include the names of qualified businesses receiving investments, the investment amount, and credits claimed. Moreover, statute for this credit dictates what is to be reported to the Legislature including number of credits issued, recipient data (name, location, line of business), total investment in the recipient business, and number and amount of credits revoked. A final review component in statute requires its Department of Employment and Economic Development contract with a qualified entity to perform a program evaluation of this particular tax credit on the state's economy by December 2012. The contractor would have one year to complete the evaluation.

In 2012, Hawaii completed a legislative audit of its high-technology business and research activities tax credits which found that for a program costing almost $1 billion in foregone revenue to the state, the state cannot measure or assess the credit's effectiveness. The audit concluded the state is unable measure the impacts of credits in order to justify losing an amount of revenue this size without legislative oversight. The audit report recommended following the Pew Center for the States model in designing effective analysis and reporting on these tax credits, removing taxpayer confidentiality to enhance reporting and transparency, and strengthening internal controls over department processes to ensure financial reporting is reliable. Similar to New Mexico, Hawaii has zero goals or performance measures written into the statute for these credits, and no requirements for information disclosure from its Department of Taxation, which refused the auditor's request for taxpayer data, making independent analysis impossible.

North Carolina has two main highly-competitive, performance-based discretionary incentive programs, the Job Development Investment Grant Program and the One North Carolina Fund. State funds are only disbursed for actual jobs created under these grants. In addition, North Carolina's recent economic development inventory is a step toward providing the tools needed to encourage better legislative and executive oversight of economic development spending. This inventory attempts to identify all state-financed economic development programs and their funding trends. The Economic Development Inventory examines several angles of the issue:

- The specific programs and tax incentives that compose the state's economic development spending and who administers these programs;
- How spending on direct incentives compares to support programs; and
- How spending breaks down among tax incentives, general fund appropriations, and transportation.

By identifying the full spectrum of programs and itemizing such figures the state can begin to assess the appropriateness, efficiency, and effectiveness of the state's economic development spending.

Tennessee recently established a website that lists businesses and incentives information for state-issued grants, tax incentives and community block grants and how many jobs the money has reportedly created.

In January 2012, *Good Jobs First*, a national policy resource center, reported on its evaluation of similar state subsidy programs in terms of disclosure, performance standards, and enforcement practices. The table below shows the top ten states in each category.

Table 6. Highest Ranked States for Accountability Standards

Disclosure		Performance Standards		Enforcement	
Rank	**State**	**Rank**	**State**	**Rank**	**State**
1	IL	1	NV	1	VT
2	WI	2	NC	2	VA
3	NC	3	VT	3	IL
4	OH	4	IA	4	MI
5	MO	5	MD	5 (tie)	AZ
6	CT	6	OK	5 (tie)	NC
7	MI	7	VA	7	MD
8	IN	8 (tie)	FL	8 (tie)	CO
9	KY	8 (tie)	RI	8 (tie)	CT
10 (tie)	LA	10	TN		KS
10 (tie)	PA				
10 (tie)	TX				

Source: *Good Jobs First Studies*

To assist economic development policymakers and practitioners in improving their subsidy enforcement practices, *Good Jobs First* offered the following policy recommendations:

- All recipients in all programs should be required to report to agencies on job creation, wages, benefits and other performance benchmarks. Recipient reporting data should be disclosed online at least annually as part of a state's disclosure system.
- All reported information should be verified by agencies using techniques such as auditing and cross-checking of company claims against separate reliable data sources such as unemployment insurance records.
- Agencies should penalize recipients found to be out of compliance, employing techniques such as recapture (clawbacks), recalibration of future benefits and rescission or termination of subsidy agreements. Programs that are performance-based should operate without penalties only if recipients are required to fulfill all programs requirements before receiving any subsidies.
- Penalty systems should be straight-forward, consistent, and not weakened by various exceptions or by giving agency officials discretion on whether to implement them.
- Agencies should publish detailed data on their enforcement activities, including the names of the recipients found to be non-compliant and those penalized, including the penalty amounts.

Recommendations

The Legislature should consider formalizing within statute

- Public disclosure requirements for businesses receiving economic development tax credits;
- Prioritizing cost-effective evidence based economic development incentives;
- Data sharing requirements between the Economic Development Department, Taxation and Revenue Department, and agencies that house information that would assist in analysis of incentives, such as the Department of Workforce Solutions.

The Economic Development Department should

- Update its performance monitoring plan to include all the required elements that are clear and specific to ensure accuracy and reliability; and
- Publishing comprehensive incentive information by recipient on its Data Center website.

The Taxation and Revenue Department should

- Research and formalize a measure of economic return to the state from job growth in conjunction with economic research resources such as the Bureau for Business and Economic Research at the University of New Mexico (BBER) or the Arrowhead Center at New Mexico State University.

The Economic Development Department and the Taxation and Revenue Department should

- Establish an inventory of all state financed economic development programs; and
- Implement a system to track all incentives given to a company by an economic development corporation, a city, a county and the state. In order to gain a clear picture of all the incentives a company is receiving, a total summary of tax incentives is necessary. A summary of a company's tax incentives from each level of government will help ensure that one company is not over incentivized.

SINCE 2007, THE STATE HAS ISSUED OVER $63 MILLION IN LOCAL ECONOMIC DEVELOPMENT ACT GRANTS, WITHOUT SAFEGUARDS TO ENSURE JOBS ARE CREATED

Overall, from 2007 to 2011, the EDD has received $63.6 million in capital outlay appropriations to provide LEDA grants statewide. The grants were distributed to various political subdivisions, and for specific economic development projects such as Schott Solar and Fidelity Investments in Bernalillo County. As of June 2012, there are 29 LEDA projects totaling $56 million, of which 19 are complete.

Table 7. Examples of LEDA Projects
(in thousands)

Project Name	County	LEDA Amount
Louisiana Energy Services	Lea	$250
Bloomfield Industrial Park	San Juan	$300
Pre-Check	Otero	$400
Ramah Meats	McKinley	$465
CFV Solar/Fraunhofer	Bernalillo	$750
Schott Solar	Bernalillo	$15,940
Fidelity Investments	Bernalillo	$14,000
Hewlett Packard	Sandoval	$12,000
Santa Fe Film Studio	Santa Fe	$10,000
Total		**$54,105**

Source: EDD

LEDA agreements do not include clawback provisions, keeping the state from recouping any funds if a company closes or reduces its workforce. Clawbacks are limited to the local entity's contributions and not state funds when the state has contributed a larger portion of the funding. The state does not have a contractual agreement with the company; clawback stipulations for state funds are not included in the intergovernmental agreements and the project participation agreements. In 2009, the LFC reported that state incentive agreements need to link incentives to performance and recommended the state require incentive clawbacks for non-performance.

Clawbacks provide taxpayers a way of making sure their investment in development incentives pays off in the form of real public benefit and allow governments to recoup their money if it does not. Clawbacks may be executed in part or in full when jobs are not created. A percentage refund, based on the number of jobs created compared to the number projected in the tax abatement agreement, is common. However, penalties are weakened by the fact that their implementation is discretionary rather than mandatory or by the presence of various exceptions. Minnesota bars companies subjected to clawbacks from receiving any incentives for five years or until the incentive is repaid. Another technique is to distribute the incentive monies after interim projections have been met and support documents have been verified. Public officials must monitor corporate performance on a regular basis, and enforce clawbacks when needed.

In December 2011, the EDD created LEDA program economic impact policies. Although the policy provides adequate guidance, it currently does not include specific requirements for measuring economic impact and does not mention any requirements for clawbacks under the LEDA grants. The EDD is currently researching and discussing various clawback provisions, but it has not revised the language in its agreements.

The state could have recovered an estimated $5.5 million from Schott Solar if a similar clawback as the city of Albuquerque's was in place for state funds. Schott Solar announced on June 28, 2012 it is ceasing Albuquerque operations in 2012, laying off 200 workers immediately and the 50 remaining employees over the summer. Schott Solar received $15.9 million in state capital outlay through LEDA grants, $1 million from the city of Albuquerque and $500 thousand from Bernalillo County. These funds were committed under a project participation agreement (PPA) with a 10-year lease, requiring Schott Solar to hire 735 employees by the end of 2014, and maintaining the 735 until 2018.

The agreement has a facility closure clawback stating should Schott cease operation of the project on or before December 31, 2018, Schott shall, within 90 days of the cessation of operations, pay to the city, in cash, an amount equal to 25 percent of the city's $1 million contribution less the amount that was contributed by offsetting application and permit fees. Any clawbacks not paid when due will bear interest at the rate of prime plus 2 percent per annum from the due date until paid. In mid-July 2012, the city sent a letter to Schott regarding the lease agreement obligations for Schott to pay the city's attorneys' fees. As of July 27, 2012, the facility had not closed; Schott is still manufacturing. The 90-day period under the PPA commences when Schott ceases operations.

In addition, the PPA clawback provisions while Schott Solar remained in business are directed to the city's contribution, not the state funds and include language for business climate changes and allow the city to waive or modify the provisions if Schott does not meet 80 percent of the target. The solar industry in the United States has been negatively impacted by a number of factors, notably the trade practices of China. As a result, Schott did not meet its employment goals for 2011 (435 for LEDA and 360 for Industrial Revenue Bond (IRB)). In May 2012, the city modified the clawback penalties, with Schott reimbursing the city $78.4 thousand ($24.5 thousand under the LEDA PPA and $53.9 thousand under the IRB). The total amount due was $261.4 thousand, but the city deferred the $182.9 thousand balance pending future compliance with the terms and conditions of the agreements. Since Schott Solar will not be in operation for the full length of time, any deferred balances will be due along with facility closure clawback penalties.

Table 8. City of Albuquerque
Schott Solar Annual LEDA Report

Date	Target # of Jobs (cumulative)	Schott Payroll FTE	FTE as a % of Target	Contract FTE	Total FTE	Total FTE as a % of Target
12/31/2009	135	179	132.6%	178	357	264.4%
12/31/2010	285	251	88.1%	46	297	104.2%
12/31/2011	435	252	57.9%	2	254	58.4%

Source: Schott Solar Status Report

Schott Solar provided annual reports to the city of Albuquerque, meeting the project participation agreement requirements showing the number of employees hired. Schott Solar reported in its 2010 annual report it uses temporary employees through the Manpower Group ("Contract FTEs") to maintain operational flexibility in light of changing business conditions. According to the city, the number of employees had not been validated, but the city has the option to review and audit Schott's records.

While the city of Rio Rancho will be tracking all of Hewlett Packard's 2012 job data, the clawback provisions begin in calendar year 2013. Hewlett Packard (HP) received $12 million in state LEDA grants along with $7.4 million in JTIP funds and approximately $2 million in other incentives from the city of Rio Rancho. HP consolidated three centers when it relocated to New Mexico, opening the Rio Rancho facility in late 2009 under a 15-year lease. HP's project participation agreement does not have an annual requirement for the number of jobs. Instead HP is to continuously employ 1,350 or more full-time equivalent employees on and after the end of calendar year 2012. The Rio Rancho City Manager stated this allowed for a three-year ramp up period. The project participation agreement does require HP to provide the city with copies of its New Mexico Workforce Solutions Department Employer's Quarterly Wage Contribution Report. HP had 1,136 employees as of April 2012, and 1,048 employees as of June 2012, with 40 percent in technical support positions and 60 percent in sales. HP has paid in excess of $196 million in employee salaries from January 2009 through June 2012.

In July 2012, HP announced it was laying off 100 workers at its Rio Rancho facility, which indicates it will not meet its employment requirements at the end of calendar year 2012. Should HP fail to meet its full-time employment requirement, the clawback provision is limited to a percentage of the annual value of the city provided incentives and does not include state funds. The clawback for the city's contribution is based on a percentage shortfall of jobs applied to the annual value of its contribution with the annual value for any given year set at 6.67 percent of the total value. Using the number of jobs as of June 2012, less the 100 laid off employees, the percentage job shortfall would be 30 percent (402/1,350) and the estimated clawback for the city of Rio Rancho would be $44 thousand for 2012. Applying a similar methodology, the LFC estimates $238 thousand in penalties could be returned to the state if a clawback provision was in place for its contribution.

Bernalillo County has not fulfilled its oversight, monitoring, and reporting responsibilities as stipulated in its agreements. In January 2009, Bernalillo County entered into a project participation agreement with Forest City, NM, LLC (FCNM) as the qualifying entity under LEDA to construct a 216,000 square foot building, and lease it to Fidelity. In turn, Fidelity would create and retain jobs within the county over a 10-year period. The state contributed $14 million in LEDA grants, with the city of Albuquerque contributing $1 million for infrastructure and a combined total of $13.3 million from Fidelity and Mesa del Sol.

The project participation agreement requires a minimum of 350 new jobs annually or 3,500 job years created cumulatively under a 10-year lease with Fidelity, with the intent to create up to 1,260 jobs by the end of 2011. The agreement requires FCNM to submit annual status reports 60 days after the end of each year that Fidelity leases the building. Fidelity reported as of May 31, 2012, it had 454 employees at the site. The job numbers for prior years were provided to the county by Fidelity. Although there are clawback provisions in the project participation agreement, they do not go into effect until the end of 2017. If Fidelity creates less than the 3,500 job-years, FCNM agrees to reimburse the county the sum of $1,000 multiplied by the number of employees less than the required number of jobs.

It is the county's responsibility to conduct annual performance reviews. When LFC requested the annual reports and annual performance monitoring reports, Bernalillo County stated a "full report" would be provided under separate cover and that it approved Forest City's request for additional time to gather the more detailed payroll information. Correspondence between the county and Fidelity indicates the county had not obtained the job creation information until June 2012 when the LFC requested it. It appears the county has not conducted annual performance reviews. As of this writing, Bernalillo County has not provided the requested information. In addition, the Memorandum of Understanding between the EDD and the county requires the county to submit bi-annual reports of direct and indirect jobs created. There was no evidence in the EDD project file indicating such reports had been submitted.

In August 2010, the county's internal audit department reported the required monthly legislative grant reports for capital outlay projects were not being completed. State grant agreements require monthly progress reports be submitted to the state Department of Finance and Administration for all legislative grants. The LEDA grant to FCNM was for infrastructure, making it a capital outlay project.

The Santa Fe Studios' $28 million project could prove to be a risky investment to the state with its $10 million contribution. Phase 1A construction was completed in October 2011. Santa Fe Studios (SF Studios) opened in November 2011, complete with a state-of-the art 19,275 square foot soundstage, dressing and makeup rooms, and office spaces. It also has an open 57-acre back lot to be used for building sets or more storage. Since opening, SF Studios has hosted one production, a television pilot for approximately three months. The project participation agreement requires SF Studios to provide 500 thousand hours of direct and indirect jobs of above-minimum wage by 2018. All construction jobs are to be credited towards the job hour requirement. The SF Studios has provided Santa Fe County two quarterly reports that include 12,348 job hours. However, the county has not tabulated the cumulative total to include the construction jobs. In addition, the production company for the television pilot has not yet submitted its job and wage reports to SF Studios.

<u>Job creation requirements vary and there are no requirements in place for job retention</u>. The 2009 LFC Brief on the Survey of Economic Development Initiatives recommended that minimum standards for both job creation and retention be established. The HP project participation agreement clearly defines the number of jobs and a full-time-equivalent as 2,080 hours per year. Examples of the various job creation requirements in other project participation agreements include:

- Job creation defined in job years and it is not always clear how many jobs are to be created.
- Target number of jobs created on an annual basis with and without a cumulative total.
- Direct or indirect number of hours within a stipulated time period or over a period of time, not specific as to number of jobs to be created.

Having different job creation requirements makes it difficult to capture benchmark data. In some instances, there are targets in the PPAs for maintaining a certain number of jobs over time, but none of the nine PPAs the LFC reviewed include specific requirements for job retention. Establishing minimum job creation and retention standards and tracking job retention would provide the EDD a foundation for accurate benchmarks.

In addition, project participation agreement job reporting requirements are not standardized. The city of Rio Rancho requires Hewlett Packard to provide New Mexico Workforce Solutions Department Employer's Quarterly Wage Contribution Report. Other PPAs rely on the company self-reporting and have not required documentation or validation of the reported information. Furthermore, the EDD does not track actual jobs created by the LEDA grant program.

Although the EDD relies on the local municipality to monitor the requirements set out in intergovernmental agreements, it does not always require the municipality to provide progress reports or job creation numbers. Reporting requirements defined in some agreements are not enforced. While local government entities are required to submit job creation reports during the life of the agreements or on a bi-annual basis to the EDD, the type of documentation required to support the jobs created is not included. There were no progress reports in the LEDA files. Also, the EDD's project files did not show evidence that the department requested the reports from the local entities and the entities have not provided them. A final report is due upon final disbursement or upon completion of the project. The term of the intergovernmental agreements expire prior to the project participation agreement term, making it difficult to determine when the reports should be submitted and when to enforce the reporting requirements.

In contrast, each Texas Enterprise Fund (TEF) grant recipient is required to submit an Annual Compliance Verification report each year through the duration of its contract term. These reports cover the status of yearly job targets and other contracted commitments and are maintained by the Office of the Governor's Financial Services division, which monitors for fulfillment of all TEF agreements. Texas Workforce Commission quarterly reports are also used as a third-party validation of employment numbers.

The Economic Development Department (EDD) monitoring and oversight of LEDA grants needs improvement. Language in the intergovernmental agreements (IGA) does not promote accountability. The IGA states "EDD shall, at their discretion, review and audit the Project if it is deemed to be necessary or desirable." The department stated "It is not required to audit but reserves the right to do so if needed; however, there has not been a reason to audit." The EDD does not maintain documentation to support its decision not to conduct reviews and audits. The department's oversight is limited, and appears to cease once the EDD processes the payment request to the local government. This was evident with the lack of progress reports in the projects files.

During the evaluation the EDD could not provide a complete listing of all LEDA grants issued from 2007 to 2012. The detail information for the 2007 appropriations was not readily available and was incomplete. The LFC relied on the appropriation laws and information in the Capital Outlay Monitoring System. Regardless of staff turnover, the EDD should adequately maintain records for its LEDA grant program.

Recommendations

The Legislature should consider formalizing within statute the following:

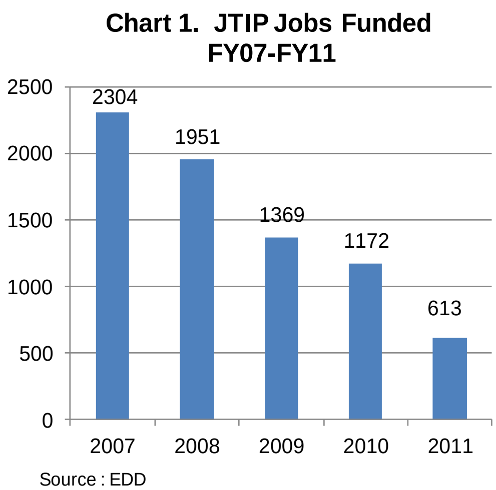
- Clawback provisions for all economic development direct expenditures to ensure clawback requirements are consistently applied.

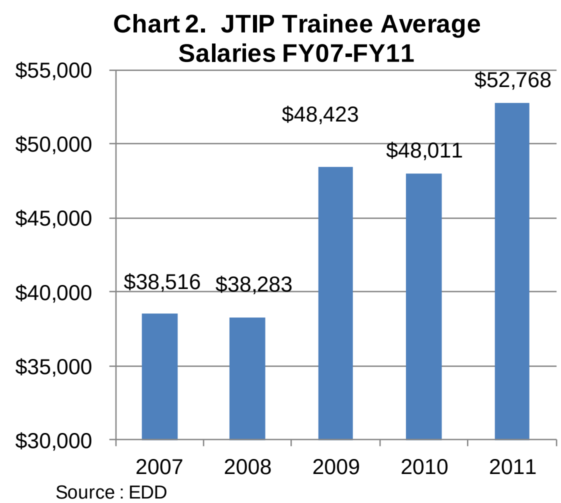
The Economic Development Department should

- Update the LEDA policies to include requirements for clawbacks.
- Include clawback provisions for state funds in its intergovernmental agreements.
- Require local entities to include clawback provisions for state funds in its project participation agreements.
- Establish a standard requirement for defining the number of jobs created.
- Include job reporting requirements in the intergovernmental agreements for the LEDA that include actual jobs created and retained, holding the local entity responsible for obtaining the information and providing the quarterly wage and contribution reports to the state to ensure accountability through the duration of the company's project participation agreement.

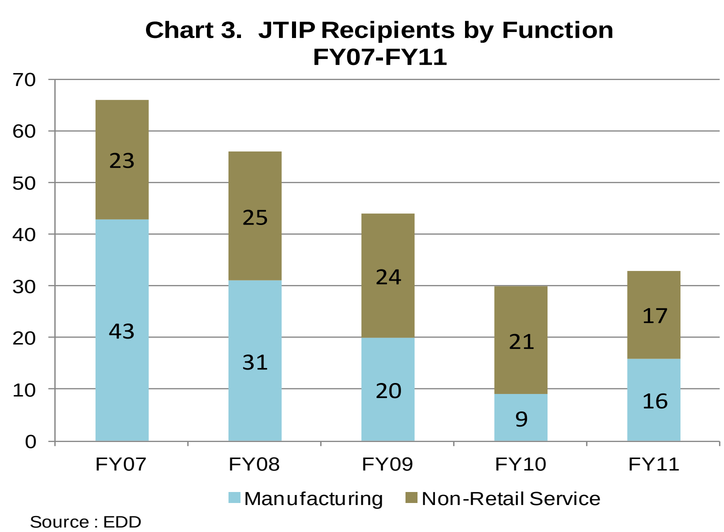
BETTER ACCOUNTABILITY MEASURES ARE NEEDED TO ENSURE THE JOB TRAINING INCENTIVE PROGRAM PRODUCES SUSTAINABLE LONG-TERM RESULTS

The Job Training Incentive Program (JTIP) provides state subsidies to help lower the cost of training employees for businesses who relocate or expand into New Mexico. The JTIP was created in 1972 as the Industrial Training Program, which focused on offsetting training costs for new manufacturers moving into the state. In FY11, the program paid out $1.2 million to support the creation of 613 jobs, 43 of which were in rural areas. Average trainee salary for FY11 totaled $58 thousand per year. The program has continued to expand to new business areas such as customer service and also added a new program area, STEP UP, to assist employers looking to provide training to incumbent workers.





Originally created to expand employment in manufacturing, the JTIP now primarily funds call center jobs. In 1993, the program updated its qualification parameters to include non-retail service sector jobs where 50 percent of business was generated outside New Mexico. This change has allowed customer service call centers to access JTIP funds. However, as the call center industry has matured in areas such as Albuquerque and Rio Rancho, it is unclear whether companies place call center operations in New Mexico because of JTIP, or because of the accessible infrastructure and a ready-made workforce, companies bring their call center operations to New Mexico in spite of available JTIP funding.



For example, America Online (AOL) closed a call center in Albuquerque in 2006, eliminating 900 jobs. Convergys, a third party call center, moved into the AOL location in 2007, projecting creation of 500 jobs. In 2010, Convergys closed down their Albuquerque operation, eliminating 677 jobs. Most recently, Lowe's Home Improvement took over the same location and projected employing 600 people. For this one location, there is a net job loss of almost 300 jobs from the activity of these three companies. Being able to look at employee movement across all call centers in the area would provide a more accurate picture of whether jobs are being created, or merely being reallocated as different organizations move in and out.

The JTIP Board passed rule changes for FY13 to expand eligibility into other business functions such as research and development and headquarters operations. In June 2012, the JTIP Board approved measures to open eligibility to new types of operations, including research & development and early stage manufacturing, as well as corporate headquarters. These new functions still have to derive 50 percent of their revenues from outside of the state, but this is the first time that JTIP has expanded into business areas that do not directly provide a product or service, but are either support or innovation-oriented.

The JTIP funds new employee training without taking previous experience into account. While JTIP uses federal Department of Labor standards for training timeframes by specific job functions, it treats every employee as if they are new to the job function they are performing. Therefore, all trainees approved will receive full reimbursement up to the maximum reimbursement rate for the participating company. In the case of both Convergys and Lowe's, they have or will receive funding through JTIP. Between 2007 and 2009, Convergys received $975 thousand to train 543 employees. Lowe's has yet to receive any reimbursement under JTIP, but has a current reimbursement budget of $1.5 million. While JTIP does not allow employees to be funded twice for training within the same organization, an employee can receive JTIP funds to be trained in various organizations over time. Therefore, it is possible that the state paid a portion of employee wages for training for similar job functions between different organizations such as Convergys and Lowe's. In contrast, on-the-job training reimbursement through the federal Workforce Investment Act requires skill assessments to determine an employee's skills gap and funds training to bring the employee in line with the requirement of their new position.

JTIP funds small and large projects alike without a prioritization that aligns with an overall state economic development strategy. Funds are currently made available on a first-come-first-served basis instead of being budgeted strategically to achieve specific goals. In the EDD FY13 strategic plan, the JTIP's objectives include increasing company participation in the program, increasing the number of jobs funded, and sustaining the quality of jobs funded, reflecting that the focus is total jobs trained as opposed to having a strategic focus for different industries in different areas of the state based on region-specific strengths. While these goals align with the EDD's mission of creating jobs and providing incentives, there is no overarching strategy for approaching job creation in the state which would guide how JTIP dollars are allocated. In Massachusetts, applicants for grants from the Workforce Training Fund are rated based a uniform rubric that aligns with the state's goals for economic development including economically depressed areas and under-represented industries.

To encourage higher-wage jobs, Arizona's job training program requires a minimum wage to be considered for funding. In Maricopa County, the largest county in the state, the minimum annual salary to participate in the program is $39,687 or $19.08 per hour. The JTIP does follow federal Department of Labor guidelines for minimum wages based on job zones shown in the table below.

Table 9. Federal Department of Labor Guidelines for Wages and Training Hours

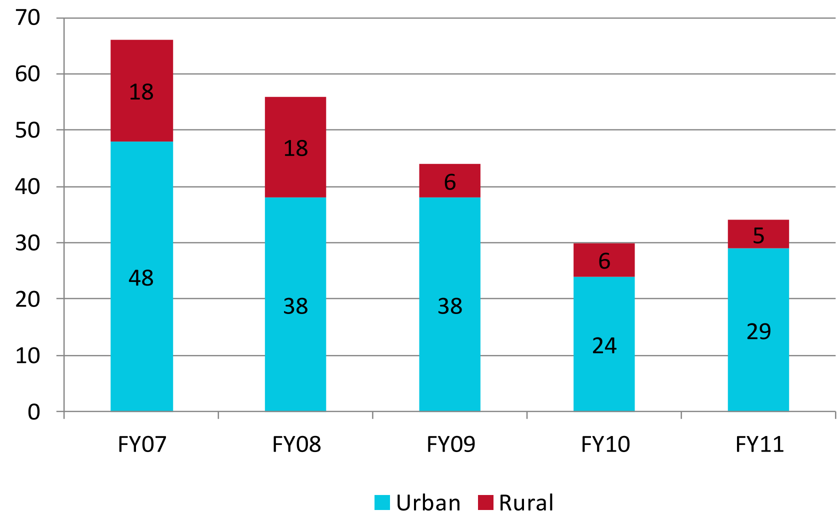
Job Zone	Definition	Training Hours	Minimum Wage at Hiring Urban	Minimum Wage at Hiring Rural
1	Little or No Preparation Needed	160	$9.00	$8.00
1a	Little or No Preparation Needed	320	$10.00	$8.50
2	Some Preparation Needed	480	$11.50	$9.00
2a	Some Preparation Needed	640	$13.00	$9.50
3	Medium Preparation	800	$14.50	$11.00
3a	Medium Preparation	960	$16.00	$12.00
4	Considerable Preparation Needed	1040	$19.00	$13.00

Source: EDD

However, this does not tie specifically to wage and labor conditions in the state, and the salaries based on this table range from $16.6 thousand to $39.5 thousand per year. While JTIP is reinstating a 5 percent premium for high wage jobs based on the parameters for the High Wage Job Credit ($40 thousand in urban areas and $28 thousand in rural areas), this additional incentive is optional for applicants.

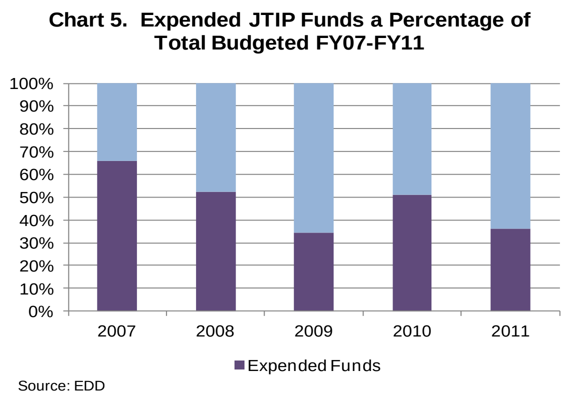
JTIP-funded jobs are located near urban centers within the state and near major transportation corridors. Since FY07, JTIP has approved $56 million in funding with 85 percent in urban locations and 15 percent in rural locations. The most projects were approved in Bernalillo County, for 5,243 positions allocating $30.4 million, followed by Sandoval ($14.6 million) and Doña Ana Counties ($2 million). Twelve counties had zero JTIP funding for employers in the past five years (refer to **Appendix D – Funding by County**). While rural companies receive a higher reimbursement (between 65 and 70 percent), most companies participating in JTIP chose to locate in urban areas (receiving up to 40 percent reimbursement.) A 2008 study published in The Review of Regional Studies concluded that availability of materials, transportation options, and high-tech support were key factors in picking a business location. However, once in a location, companies considered local supply of skilled labor, local tax structures, and lower relative labor costs as significant in the decision to relocate.

Chart 4. JTIP Urban and Rural Recipients FY07-FY11



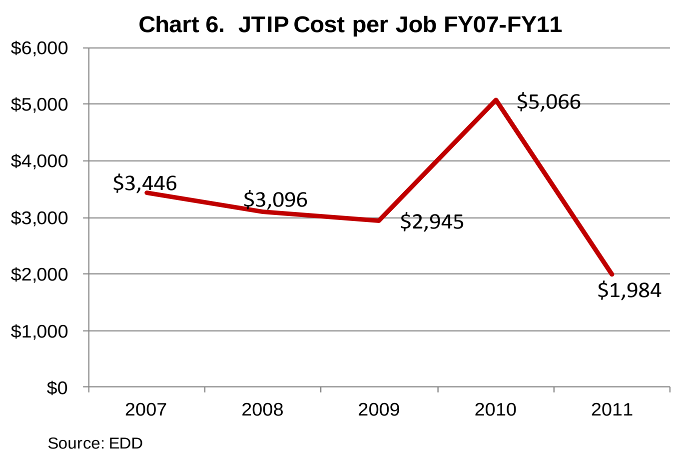
Source: EDD

<u>**The JTIP has only spent half of the funds encumbered to reimburse companies between FY07 and FY11.**</u> The JTIP paid $25 million in reimbursements of a total $50.2 million encumbered between FY07 and FY11, 50 percent of funds budgeted for reimbursement to participating companies. When companies apply for JTIP funding, they provide an estimate of jobs they look to fill and create a reimbursement budget based on the average wage for these positions. These job numbers have been amended during the contract period. In some cases, companies amended job totals down to address hiring challenges. Also wage rates were adjusted either up or down to better address market rates for similar job duties. These amendments account for actual reimbursement payments being less than originally budgeted. The economic recession contributed to this underutilization, but other factors in how the JTIP is designed contributed as well. While unexpended funds are eventually unencumbered and returned to the overall JTIP budget, this 50 percent differential in budgeting may prevent other applicants from being able to access funds. The JTIP could address this issue by placing minimum requirements on jobs created and tying these to milestones through the one-year reimbursement period, or consider encumbering only portions of the total reimbursement budget as jobs are filled. Addressing this budgeting variance would allow JTIP funds to be leveraged more effectively by more recipients.



The JTIP Board also used FY13 funds to reinstate reimbursement rates reduced due to lack of funding. After funding reductions in FY10, the JTIP Board reduced the reimbursement rate for urban recipients to 40 percent, eliminated the additional 5 percent reimbursement for high wage jobs, and cut the travel reimbursement for training. Urban reimbursement has been changed back to 50 percent, and the high-wage differential and travel reimbursement have been re-implemented for FY13.

The JTIP costs more than other similar programs, according to FY10 data. The JTIP cost per job was steady near $3,000 for FY07-FY09, but dramatically increased to $5,000 in FY10, at the height of the economic recession. For FY11, the cost was the lowest for the period of FY07 through FY11 at $2,000, with an average salary of $52.8 thousand, but only 613 jobs were created. Average wages for JTIP recipients grew from $38.3 thousand per year to $48.4 thousand, a 26 percent increase between FY09 and FY10, which would drive up the cost per job reimbursed. In the case of the Texas Workforce Commission Skills Development Fund, which is similar to JTIP, the cost per job was $1,190.



<u>JTIP performance measures do not meaningfully assess the effectiveness of the program.</u> The JTIP has had various AGA performance measures over the last few years, as detailed in the table below:

Table 10. JTIP Performance Measures FY11-FY13

Measure	FY11 Target	FY11 Result	FY12 Target	FY12 Result	FY13 Target
Number of workers trained by JTIP	2,000	553	2,000	1015	1,000
Percent of employees whose wages were subsidized by JTIP	60%	47%	60%	72%	60%
Number of businesses participating in JTIP	16	34	16	32	16
Number of rural businesses participating in JTIP	8	8	8	9	8
Average annual cost per job per JTIP trainee	$2,500	$5,935	$2,500	$4,600	$2,500
Average hourly wage of jobs funded by JTIP	N/A	N/A	N/A	N/A	$16/hr

Source: Performance Based Budgeting System

These measures have sought to quantify productivity, cost, employee retention, and employee wages. While some of these measures provide good demographic data about program participants, they do not speak to the effectiveness of the program in achieving economic development goals. Based on rules and practices within JTIP, only two of these measures are directly affected by the program. Number of workers trained, percentage of employees who were subsidized, total number of businesses and rural businesses are all driven by the company applying for JTIP funds. Because applicants do not have to go through a competitive process to receive funding, there is no motivation to adjust these factors to meet state economic development goals and JTIP does not place requirements for some of these parameters to be eligible for funding.

To establish meaningful performance measures for JTIP, the EDD must decide what the program should achieve. It is the Job *Training* Incentive Program, a subsidy to help *train* new employees or improve skills of current employees. Companies looking to locate in New Mexico may consider JTIP an attractive incentive to bring new jobs to the state, and if that is the true goal of the program, then JTIP should be redefined as a recruitment incentive. However, if JTIP is intended as a workforce training program, then performance measures cannot be tied to one company or only measured for the length of the one-year contract period. Performance measures and reporting should be tied to the worker to measure program benefit over the long-term in areas such as earning potential and ability to avoid needing state public assistance programs. This type of analysis could be performed with data residing at the Workforce Solutions Department or the Human Services Department.

JTIP has a clawback provision, but has never clawed back funds since the provision was introduced in 2007. JTIP reserves the right to claw back funds if eligibility for the program changes after the fact. For example, if it is discovered that employees being funded through the program dropped out of school, then any funds paid to the recipient company for that employee would be eligible for clawback. Between 2007 and 2011, five JTIP recipients were terminated due to not meeting JTIP requirements for reimbursement. Of those five, two companies closed, including Eclipse Aviation, and two companies did not provide final audit documentation to the EDD. Only ABQ Direct Inc. received reimbursement from the program for $5,760, but the EDD did not claw back these funds.

Table 11. JTIP Projects Closed for Non-Compliance
FY07-FY11

FY	Company	City	Reason for "Closed" Status
2007	ABQ Direct, Inc. DBA InnPoints Worldwide, Inc.	Albuquerque	Did not submit final audit documentation-project closed in database and company is not in good standing with the program.
2008	Eclipse Aviation Corporation	Albuquerque	Company laid off employees and declared bankruptcy. Referred to EDD legal counsel for follow-up.
2008	GUNA, Inc.	Albuquerque	Non-responsive. Company closed before completing the final audit.
2009	WorldScape, Inc.	Los Alamos	Project was approved on condition that the company provides verification of receipt of $1.5 million capital infusion within 60 days. The information was not provided.
2009	Solstar Energy Devices	Albuquerque	Compliance review revealed company was not in compliance--the trainee hired did not meet the program eligibility requirements.
2010	Visible Light Solar	Albuquerque	Did not submit final audit documentation-project closed in database at the end of the contract period.

Source: EDD

<u>The JTIP generally has adequate controls, but audit and compliance reviews need strengthening.</u> All companies receiving JTIP funds are contractually required to receive a compliance review from JTIP, as well as submit to an audit at the end of the contract period. Both of these are good control measures, and documentation of both reviews is retained by the EDD. Payments are not sent to recipient companies unless they conform to both of these requirements. In the JTIP review, the contracted compliance officer reviews payroll records, confirms trainees meet eligibility requirements, and also interviews employees to learn about training and work tasks. Prior to receiving final reimbursement for JTIP, recipient companies are required to submit to an audit by a licensed auditing firm, in compliance with generally accepted auditing standards.

Review of contract files showed audits submitted by JTIP recipients consistently do not include findings or opinions issued by the contracted auditing firm, not meeting the contractual requirement for a full audit. Various examples were identified where the independent audit did not issue an opinion stating that the recipient company was in compliance with the JTIP requirements or that calculation of reimbursement requests were accurate. Instead, the audits included standard language stating that the audit firm was not engaged to conduct an audit or state an opinion, and that the report was for the company's information only.

Furthermore, the JTIP contract does not require a detailed invoice or a contract stating the audit's scope of work be provided to the EDD. Therefore, the department has no visibility to the tasks the auditor was contracted to complete or the cost of their services compared with what the program reimburses for this service. As part of the JTIP request for funding, the program reimburses a predetermined amount for costs associated with performance of the independent audit.

There are no specified standards for determining the frequency of JTIP compliance reviews. The contract between the EDD and JTIP recipients states at least one compliance review is required before the first claim for reimbursement can be paid. It is the EDD's responsibility to conduct these compliance reviews, which are performed by an EDD contractor. The JTIP program does not have a standard process for determining frequency of review. Some recipients are reviewed repeatedly during the same project, while others are reviewed only once. The program determines frequency of review on a case by case basis, using subjective criteria and staff's professional judgment. This creates risk for complacency and lack of accountability.

The JTIP contracted compliance officer's services contract does not specify minimum requirements for conducting reviews of JTIP recipient companies. The EDD contracts a compliance officer to perform reviews of JTIP recipients, including meeting with human resources personnel and reviewing documentation to confirm compliance with the program. The professional services contract does not specify what the contractor needs to review, nor states any measures to assess the contractor's performance. Review of the JTIP files indicated the contractor adheres to a consistent reporting format, but the review's scope is not clearly detailed in his contract, therefore thoroughness or overall performance is not measurable.

Recommendations

The Economic Development Department should

- Institute state-specific minimum wage and job count requirements to fully access JTIP reimbursement to drive economic development goals for the state;
- Specify in the JTIP compliance officer's professional services contract a scope of work and performance measures;
- Require JTIP recipient companies to report on job retention and wages for a period of time after final reimbursement for longitudinal analysis, such as three to five years;
- Revise JTIP training hour calculations to consider previous work experience, similar to federal Workforce Investment Act requirements; and
- Revise the JTIP contract with recipients to establish what is required from the independently-contracted audit.

THE TAXATION AND REVENUE DEPARTMENT CANNOT ACCURATELY MEASURE FOREGONE REVENUE OR IMPACT FROM TAX EXPENDITURES DESIGNED TO SPUR ECONOMIC GROWTH

The TRD does not routinely review and report effectiveness of economic development tax credits to the Legislature, which is inconsistent with best practices, and in some cases, does not comply with statute. As part of this evaluation, the LFC staff reviewed five tax expenditures related to economic development: the High Wage Jobs Tax Credit, the Rural Job Tax Credit, the Technology Jobs Tax Credit, the Investment Credit, and the Research and Development Small Business Tax Credit.

Table 12. LFC Reviewed Economic Development Tax Expenditures

Tax Expenditure	FY12 Foregone Revenue	Average Credit per Claimant
High Wage Job Tax Credit	$48.1 million	$17 thousand
Rural Jobs Tax Credit	$224 thousand	$45 thousand
Technology Jobs Tax Credit	$5.9 million	$25 thousand
Investment Credit	$1 million	$16 thousand
Research and Development Small Business Tax Credit (Based on FY09 data)	$108 thousand	$1.6 thousand

Source: TRD

Per state statute, the TRD is required to report to the Legislature on the effectiveness of various tax credits, but to date has not complied with this requirement. The Investment Credit, the Technology Jobs Credit, and the Rural Jobs Credit have statutory reporting requirements to demonstrate their effectiveness to the Legislature; however the TRD has not met this reporting requirement. For the Rural Jobs Tax Credit, the WSD and the EDD are required to evaluate and report on the credit in conjunction with the TRD, but none of the three agencies could produce a report for this credit that had been presented to the Legislature. The TRD states that the Tax Expenditure Report expected to be delivered in FY13 should satisfy this requirement, but the department does not have a regular review process in place at this time to meet the annual reporting requirement.

The state does not have an established regular timeline for evaluating tax expenditures. While some credits do have requirements for review within statute, this does not span all credits. Similarly, while some credits such as the High Wage Jobs Tax Credit have sunsets, New Mexico does not have universal sunset provisions for tax expenditures. Evaluation timelines and sunset provisions both induce creating a timely process for reviewing tax expenditures.

The TRD does not have a system for collection and analysis of tax expenditure data, limiting its ability to measure effectiveness and inform the Legislature. A 2011 LFC evaluation of healthcare tax expenditures noted the TRD does not have a way to accurately measure tax incentives due to a lack of information required on taxpayer reporting forms. In the case of the economic development tax expenditures reviewed for this evaluation, data was available, but the TRD does not have a method for cataloguing the data and performing analysis electronically. For example, the High Wage Jobs Tax Credit and the Investment Credit all require the taxpayer to qualify for the credit by submitting an application to the TRD. Additionally, the taxpayer has to include a specific form with tax returns to claim the credit. These forms provide a great deal of data that could be used to measure how the tax credits perform. However, LFC staff does not have statutory authority to access the data needed to assess the effectiveness of these expenditures.

In the case of the High Wage Jobs Tax Credit, between the initial certification request and the credit application, the TRD retrieves data on the exact amount of jobs qualifying as high wage and the exact amount of the credit being claimed, the name and location of the business, the date the job was created, whether the employee is a New Mexico resident, and whether the job is located in an urban or rural area. This data could be used to perform the type of analysis the Pew Center recommended in its report, however the department does not have a process or the resources necessary to take this data from paper forms to an electronic format in order to perform analysis. While the TRD has stated that forthcoming upgrades of the Gentax system would provide a platform for recording and analyzing data, currently any type of data collection and analysis is a manual process, making it time-consuming and at greater risk for error.

The High Wage Job Tax Credit has grown from $9.3 million to $48.1 million, or 520 percent between FY11 and FY12, at a time of minimal job growth. The credit's recent increase makes it comparable in size to the Film Production Credit, raising similar concerns over future unchecked growth. Constituents have voiced their concerns in other interim committees over potential loopholes in the language of the HWJTC statute, creating potential gray areas in claiming and administering the credit. In testimony before the Revenue Stabilization and Tax Policy Committee, Albuquerque Economic Development (AED) identified four areas to be addressed:

- *Definition of Wages*: Currently wages and employer-paid benefits can be used as the benchmark for salary, but there is not a clear definition of which benefits can be included.
- *Wage Rates:* The fixed wage rates of $40 thousand for urban jobs and $28 thousand for rural jobs may not reflect current market rates and not fit a high wage definition in 2012 and beyond.
- *Lack of Time Limits*: While statute states that the credit can be claimed for a maximum of four years, there are no requirements as to how far back the credit can be claimed. For example, a company that may not have previously claimed the credit for a job created in 2004 could claim the credit in 2011 and for the three following years. The TRD stated this type of retroactive filing has contributed to the growth in the credit. Of over $34 million in tax credits that have been approved for FY12, 67 percent can be tied back to FY07 through FY09.
- *Sunset Provision*: The credit expires at the start of FY16, and the AED proposes an extension to FY21.

The AED also testified that during this interim, representatives from the EDD, the TRD, the Department of Finance and Administration, and the economic development community are convening to draft legislation to address some statutory issues surrounding the High Wage Jobs Tax Credit.

Statutory definitions of rural locations for tax credits could unintentionally punish taxpayers for population growth over time. The Rural Job Tax Credit defines a rural job as first being in a designated rural area, defined by distance from an urban area, and whose location has a population below 15 thousand residents. If a rural location's population increases beyond the 15 thousand resident benchmark, a taxpayer's credit is reduced by half. While the intended goal of the Rural Job Tax Credit is to incentivize job creation in rural areas, fixed population benchmarks can have an unintended negative effect on the taxpayer who has no control over general population growth. For example, Las Vegas' population in the last census was 14.4 thousand, and by the next census, Las Vegas could exceed the 15 thousand resident guideline, therefore reducing the credit eligible taxpayers could receive by 50 percent.

In the case of the High Wage Jobs Tax Credit, the wage definition for high wage jobs differs between rural and urban areas, with a $40 thousand per year job being considered high wage in an urban area and $28 thousand for a rural area. The statute defines rural versus urban based on a 40 thousand resident population. This definition is also based on the most recent census data, which means that as rural populations grow, they could be negatively impacted by higher standards to be eligible for the credit. For example, Clovis has a current population of 38 thousand residents, qualifying businesses as rural under the current statute. However, if the population were to grow over 40 thousand before the next census in 2020, businesses would have to create jobs paying $40 thousand per year to continue to qualify for the credit.

Recommendations

The Legislature should consider formalizing within statute the following:

- Sunset provisions for economic development tax incentives, including regular review of fixed wage and population definitions for credit eligibility; and
- Guidelines for reporting on all tax credits to the Legislature to create uniformity in information being reported and frequency of reporting.

The Taxation and Revenue Department should

- Follow current statutory requirements on the reporting of economic development tax expenditures;
- Establish criteria for tax expenditure analysis using recommendations from the Pew Center for the States as a guide; and
- Catalog paper tax return data so that it can be more easily accessed for longitudinal study of tax credits.

NEW MEXICO ECONOMIC DEVELOPMENT Department

SUSANA MARTINEZ
GOVERNOR

JON BARELA
CABINET SECRETARY

August 20, 2012

Sen. John Arthur Smith
Chairman
Legislative Finance Committee
325 Don Gaspar
Suite 101
Santa Fe, NM 87501

Dear Sen. Smith,

To follow is the response of the Economic Development Department ("EDD") to Report #12-08 to the Legislative Finance Committee ("LFC") regarding EDD and Taxation and Revenue Department ("TRD") Job Creation Incentives. I note that EDD received only drafts of the report before this response was due. The response therefore does not address any changes that were made after EDD's exit interview with LFC staff on August 15.

Inaccuracies in LFC Report

The LFC report contains a number of inaccurate statements that I feel must be corrected for the LFC to have a complete and accurate understanding of the incentives discussed in the report. I would have welcomed the opportunity to discuss these mistakes with the LFC's staff. Unfortunately, I only received a copy of the report, in draft form no less, when my staff and I arrived for the "exit interview" with the LFC staff. Obviously, we were not in a position to discuss in detail a report we had been handed minutes earlier.

The LFC report, at page 12, defines a tax expenditure as "a method to advance policy through the tax code by incentivizing taxpayer behavior." In its findings and recommendations, the report then assumes that taxpayers do not change their behavior in response to incentives. It examines the costs of various tax expenditures in great depth but entirely ignores the benefits, assuming that taxpayers behaved as they would have if the incentive did not exist. For example, the LFC report makes no mention of the increase in revenue realized by the jobs created by these incentives or the businesses that relocated to or expanded in the state. In order to have a comprehensive approach for financing and monitoring the performance of job-creation incentives, for which the LFC report indicates the state should strive, one must quantify the benefits of tax expenditures as well as their costs.

Page 14 of the LFC report—the first page of the Findings and Recommendations section and the first page of the draft report that was provided to EDD—describes a 2009 LFC brief in which "staff identified various areas of concern in the execution and monitoring of economic development incentive programs

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including inconsistent or incomplete data, programs fragmented between agencies, and lack of a statewide economic development plan and clawback provisions for noncompliance." In particular, LFC staff made five recommendations in 2009 to improve effectiveness and accountability in economic development programs: 1. Prepare a statewide economic development plan that includes a variety of high performance measures; 2. Require incentive agreements; 3. Link incentives to performance; 4. Establish minimum wage standards for job creation and retention requirements; and 5. Require incentive recapture (clawbacks) for non-performance.

The report states,

> While the Economic Development Department (EDD) has implemented portions of these recommendations, the majority of them have not been addressed, leading to programs being utilized as subsidies instead of performance driving incentives, as well as no recourse for the state to recuperate [sic] funds, causing losses to the state totaling tens of millions of dollars.

In fact, EDD has implemented each of those five recommendations where appropriate. In the case of establishing minimum wage standards for LEDA projects, EDD has deliberately refrained from implementing that recommendation for reasons discussed below.

The first recommendation was to prepare a statewide economic development plan that includes a variety of high performance measures. EDD annually updates its strategic plan—its contribution to the five-year statewide economic development plan required by the Economic Development Department Act, NMSA 1978, §§ 9-15-1 through 9-15-56. Pursuant to NMSA 1978, § 9-15-12, however, approval of the economic development plan is the duty of the Economic Development Commission. EDD could not unilaterally implement the economic development plan as recommended by the LFC report.

The second recommendation was to require incentive agreements. I assume that this recommendation refers to incentives such as LEDA capital outlay grants and JTIP, and not other tax expenditures. Because the criteria to qualify for a tax incentive are defined in statute, EDD could not legally impose additional requirements for a company to qualify for a tax incentive. EDD requires incentive agreements for both LEDA capital outlay grants and JTIP funding. It is worth noting, however, that while the LFC report recommends that EDD require incentive agreements for LEDA capital outlay grants, the statute enacted by the legislature only requires an incentive agreement between the local government and the qualifying entity. NMSA 1978, § 5-10-10. Thus, while the LFC report states that EDD has not implemented this recommendation, it is in fact a recommendation for a legislative change.

The third recommendation was to link incentives to performance. As you are undoubtedly aware, EDD not only links incentives to performance, but is constitutionally required to do so. Incentives that are not linked to performance would violate the Anti-Donation Clause of the New Mexico Constitution. EDD may only create new job opportunities by providing land, buildings or infrastructure for facilities to support new or expanding businesses if this assistance is granted pursuant to LEDA. N.M. Const. Art. IX, § 14. LEDA requires that the qualifying entity enter into a project participation agreement that

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requires of the qualifying entity a substantive contribution of value, security, and the pledge of the qualifying business's financial or material participation and cooperation to guarantee the qualifying entity's performance pursuant to the project participation agreement. NMSA 1978, § 5-10-10 (1993).

The fourth recommendation was to establish minimum wage standards for job creation and retention requirements. JTIP agreements include wage standards for both job creation and job retention requirements. LEDA agreements do not, and for a good reason. The LEDA projects funded by direct appropriations from the legislature have been exclusively located in Albuquerque, Rio Rancho, and Santa Fe. By contrast, EDD's LEDA efforts focus on the state's rural areas so badly in need of improved infrastructure and increased capacity. Only four projects—$2,550,000 of the $25.7 million appropriated to EDD and committed to a project through its vetting process—were located in Albuquerque, Rio Rancho, Santa Fe, or Las Cruces. Every other LEDA project is located in a rural area. Those projects are simply not going to locate in Las Vegas, Espanola, Deming, Portales, Jal, Reserve, Alamogordo, Bloomfield, Ramah, Gallup, Hagerman, and Questa—as EDD's LEDA projects have—if the businesses will be required to pay Albuquerque-level wages. The unintended consequence of establishing a minimum wage standard for LEDA capital outlay grants would be to drive every project to the Albuquerque, Santa Fe, or Las Cruces metropolitan areas.

The fifth recommendation was to require incentive recapture (clawbacks) for non-performance. This will be discussed in greater detail below, but every economic development incentive administered by EDD includes clawbacks. Every JTIP agreement includes a clawback. Every LEDA agreement entered into during this administration has included a clawback. Every LEDA agreement entered into since the 2009 recommendation has included a clawback with the exception of Schott Solar, which will also be discussed in detail below.

Thus, contrary to the assertion on page 14 of the LFC report, EDD has implemented each and every one of the recommendations in the 2009 report. Given the nature and tenor of the statement in the LFC report, I would appreciate knowing its basis.

Likewise, page 21 of the LFC report states, "Clawback stipulations for state funds are not included in the intergovernmental agreements and the project participation agreements." That is simply false. Every PPA executed during this administration that appropriate state funds to an economic development project included a clawback provision. Every PPA executed in the last administration included a clawback provision, except for Schott Solar. The statement on the same page that "[c]lawbacks are limited to the local entity's contributions and not state funds when the state has contributed a larger portion of the funding" is true only of the Schott Solar deal. It is not true of the other LEDA projects.

It is interesting that the LFC report only examined economic development tax expenditures since 2007. Whether selected deliberately or not, this time frame ignores EDD's efforts to reform the economic development incentive process. In April 2006, EDD completed a *Survey of Business Incentives Assessment Methodologies and Best Practices* and presented it to the LFC. Among the research goal recommendations of that 2006 survey were to gauge the public costs and benefits of the incentives, the percentage of companies meeting compliance standards, the perspective of eligible companies who have

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and who have not used the incentive, how consistent each incentive is with New Mexico's economic development strategy and the good of the state, the impediments to gathering and reporting data on the part of businesses participating in the incentives and especially to determine if small businesses and rural areas will be impacted disproportionately with large corporations in urban areas. The 2006 survey recommended legislative changes regarding proprietary information necessary for a full assessment of incentives and information sharing among agencies, a "total system" approach to evaluating incentives, and simpler reporting requirements that increase the chances of obtaining accurate data. Although the 2009 and present LFC reports include many similar recommendations, none of EDD's 2006 recommendations have been enacted.

The LFC report must also be viewed in its appropriate context. The LFC report implies an excessive use of capital outlay on economic development projects. Capital outlay for LEDA grants, JTIP, and tax incentives are necessary for New Mexico to compete to recruit new businesses and retain existing ones for two reasons. First, these incentives are necessary because the state's tax climate is so poor. In 2012, the Tax Foundation ranked New Mexico's business tax climate 38th in the nation, despite the fact that the state has the lowest per capita property tax in the nation. The Ernst and Young study you have undoubtedly become familiar with found that New Mexico had the single highest tax burden on new business investment in the nation. Numerous incentives are only necessary because New Mexico taxes goods and services that surrounding states do not.

The Investment Credit Act, NMSA 1978, §§7-9A-1 through 7-9A-11, is the perfect example. On page 43, the LFC report finds that this incentive resulted in $1 million in foregone revenue in 2012 and more than $11 million as recently as 2009. It is certainly true that New Mexico foregoes the compensating tax on qualified equipment imported into the state for use in a manufacturing operation. Far less, if any, of that equipment would be imported in the absence of the credit, however, because only one of New Mexico's neighboring states taxes that equipment in the first place.

Many Neighboring States Exempt Sales Tax on Transactions While NM Collects GRT

State	Manufacturing Machinery	Utilities	Transportation Services	Repair Services	Professional & Personal Services	Custom Software
Arizona	Exempt	Taxable	Taxable	Exempt	Exempt	Exempt
Colorado	Exempt	Exempt	Exempt	Exempt	Exempt	Exempt
Nevada	Taxable	Taxable	Exempt	Exempt	Exempt	Exempt
New Mexico	Taxable*	Taxable	Taxable	Taxable	Taxable	Taxable
Oklahoma	Exempt	Exempt	Taxable	Exempt	Exempt	Exempt
Texas	Exempt	Exempt	Exempt	Taxable	Taxable	Taxable
Utah	Exempt	Exempt	Taxable	Taxable	Exempt	Exempt

*New Mexico offers the Investment Tax Credit to offset a percentage of the cost of manufacturing machinery.

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Source: www.taxfoundation.org

Second, these incentives are necessary because the Anti-Donation Clause prohibits direct contributions to companies as a recruiting mechanism. New Mexico is surrounded by states with large "closing funds." Arizona, Colorado, and Texas all have substantial access to cash to recruit industry. Texas's closing fund exceeds $400 million. The State of Texas, the City of Austin, and Travis County recently committed nearly $30 million in cash to locate an Apple assembly facility that will create 3,600 jobs over ten years. Even the reporting and tracking of incentive programs is impacted. The "benchmark" states mentioned in the LFC report also spend hundreds of thousands of dollars annually to produce a reliable assessment of their tax incentive programs. These funds are legislatively appropriated for that purpose.

Pages 16 and 17 of the LFC report describe how EDD "reports the number of jobs created based on company reports of anticipated jobs, not actual jobs created." EDD reports three-year projected employment when companies are relocating from out of state taking into account construction time, relocating staff, and other factors. Jobs created by business expansions and start-ups are reported as immediate hires only.

The cost-per-job calculations on page 17 and 18 of the LFC report are inaccurate for several reasons. First, as is actually discussed elsewhere in the report, EDD cannot access information regarding the use of some incentives. EDD is therefore unaware of many of the companies utilizing tax credits and cannot report on or include these jobs in its performance numbers. Second, the fiscal year in which EDD reports the new jobs is rarely the same fiscal year in which the revenue is foregone. Finally, the LFC report includes the Film Production Tax Credit to determine the total foregone tax revenue. The Film Production Tax Credit alone constitutes the majority of the economic development tax expenditures and other incentives referenced in the LFC report. EDD does not include film and media industry jobs in its job creation numbers, however. Those numbers are reported separately. The LFC report includes the cost of the Film Production Tax Credit but not the jobs that credit creates. The LFC report's analysis of the cost per job is therefore wildly inaccurate.

JTIP

On page 25, the LFC report states, "[o]riginally created to expand employment in manufacturing, the JTIP now primarily funds call center jobs." JTIP funds two categorizes of projects: manufacturing and non-retail service-based businesses. While call centers were one of the industries targeted by EDD in the early 1990s, fewer call centers have relocated to New Mexico over the past five years. Because of the success of recruiting call centers in those years, New Mexico has successfully landed a Fortune 10, information technology support center, due in part to the strong workforce which grew from the thousands of jobs which were created in the late 1990s and early 2000s. While the LFC report indicates that jobs are being reallocated as different organizations move in and out, anecdotal evidence supports the fact that career advancement opportunities have been created for the individuals who were call center employees ten years ago.

While JTIP categorizes companies other than manufacturing as non-retail service based businesses, not

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all are call centers. Other types of businesses in that category include software development and engineering services (e.g. Deep Web Technologies, Ideum, ClosedWon, JackRabbit Systems, MIMICS, CPFD Software, HACH Company, National Technical Systems), research and laboratory testing (e.g. Mind Research Network, Genzyme Genetics, Lovelace Respiratory Research Institute, Stolar, CFV Solar Testing, Vibrant), aircraft repair and refurbishing (e.g. AerSale, AeroMechanical Industries), shared-services facilities and central business offices (e.g. Lovelace Health System Central Business Office, QinetiQ), distribution centers and mail-order houses (e.g. Menlo Logistics, Prime Therapeutics), and background check industries (e.g. PreCheck).

The JTIP board reviews and makes policy changes annually. The Board consciously made changes to the call center polices in order to minimize JTIP support for lower-paying, third-party call centers. These types of call centers now must meet 90% of the county median wage to qualify. As the LFC report points out, the JTIP board has expanded eligibility to attract R&D and headquarter operations as a way to broaden utilization and target higher paying industries.

On page 27, the LFC report states, "JTIP funds small and large projects alike without a prioritization that aligns with an overall state economic development strategy." JTIP has explored many ways to better administer and prioritize the funds, while trying to meet the hiring needs of businesses. Since EDD's mission is to create jobs, it cannot earmark funds for one industry in anticipation that another, better aligned with EDD's mission, might add jobs at a later date. This type of system would almost certainly result in the loss of job creation opportunities. EDD's mission does not always align with communities that are also trying to recruit and expand businesses. Local economic development organizations have their own economic development strategies, which may or may not align with EDD's, yet the economic development directors utilize JTIP as one of the primary incentive tools to recruit and expand industries.

If the LFC's research found a better mechanism, the JTIP board and staff will be happy to learn ways to improve a priority/selection process. The JTIP board explores policies and procedures every year and has discussed this idea in the past, but has not been able to identify a better system. However, by adapting policies, the JTIP staff has found that companies make decisions to increase wages in order to access additional training hours. Policy changes impact outcomes.

The LFC report asserts, as page 28, that JTIP has only spent half of the funds encumbered to reimburse companies between FY07 and FY11. As part of the JTIP proposal process, a company is required to set a budget based on a four-month hiring projection. That budget includes the total number of requested jobs, training hours, and wage ranges for each job classification. The program's budget is set based on the mid-point of the wage ranges and establishes the estimated reimbursement amount. JTIP only reimburses companies for actual wages paid within the approved wage range, however. Once approved, JTIP enters into a contract with the company for the approved amount. Once the contract is in place, DFA requires that the funds be encumbered. At the end of the four-month hiring period, the JTIP staff requires the company to submit a hiring report which includes a roster of individuals hired, their job titles, and wage rates. If EDD discovers only a portion of the employees are hired, the JTIP staff reduces the contract accordingly, which allows for reallocation of funds for other projects. The four-month hiring requirement is set through policy and was amended to four months from six in order to free up the

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funding in a timelier manner. This policy operates as a form of clawback for non-performance.

The LFC report reviews similar programs from several other states and concludes that "JTIP costs more than other similar programs, according to FY10 data." The LFC report compared JTIP to the Texas Workforce Commission Skills Development Fund, and indicated that the Texas program is administered at a lower cost, but did not provide the number of jobs funded per fiscal year, the average wage, or the exact formula for establishing the Texas budget.

It is important to explain the JTIP formula and how New Mexico's program is administered. JTIP's budget is based on the total number of jobs (based on a 4 month hiring estimate), multiplied by the allowable training hours, multiplied by the estimated average wage, multiplied by the reimbursement percent specific for the area (rural/urban/economically distressed).

Example:
100 jobs x 800 (training hours) x $15.00/hour x .50 (urban) = $600,000
100 jobs x 800 (training hours) x $18.00/hour x .65 (rural) = $936,000

JTIP's cost per trainee increases as wages increase and when companies locate in economically distressed or rural areas of the state. The formula, which is based on higher wages and rural locations, is what drives the cost up. JTIP should not be penalized for funding higher wage and rural based projects.

The LFC report states, "JTIP has a clawback provision, but has never clawed back funds since the provision was introduced in 2007." JTIP Policy states, "If a facility that received JTIP funds closes or if layoffs of JTIP trainees occur within 1 year of the completion of training, the JTIP Board will require the refund of the funds associated with any JTIP trainee(s) which were claimed and subsequently laid off. Layoff is defined as a separation of an employee from an establishment that is initiated by the employer as a result of market forces or other factors not related to employee performance. The board will require a refund of funds from companies whose JTIP layoffs exceeded $100,000 of reimbursement. The board will require a refund of funds within 90 days of notification."

The clawback language was added to JTIP Policy in FY07. Since then, only Eclipse Aviation has met the clawback criteria. There have been instances where findings were made through the course of compliance reviews or final audits and funds have been recovered from companies, however. Since 2007 JTIP staff has collected $234,635 for 30 "overclaims," five between 2009 and 2010. JTIP staff has made a concerted effort to reduce the number of overclaims by implementing more standardized practices in claims and compliance reviews.

Beginning on page 30, the LFC report reviews the audit and compliance process for JTIP. JTIP staff credits the drastic reduction in the number of compliance review and audit findings associated with overpayment of funds to its improved practices and procedures pertaining to claim and compliance reviews. Prior to 2008, compliance reviews were done at least once at any given time during the course of the one-year project/contract period. Since then all companies have been required to conduct a compliance review upon submission of the first claim for reimbursement. The claim is not paid until the

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compliance review has been completed with no findings.

JTIP companies are required to undergo a "final audit" by an approved third-party accounting firm in order to receive payment for the final claim for reimbursement and close out the project in good standing with the program. The audit requirements and standard list of what items are to be included in the Auditor's report are outlined in the JTIP Project Closeout Audit Guide, which companies provide to the audit/accounting firms. This is the basis of the Engagement and Agreed-Upon Procedures between the JTIP company and the audit/accounting firm.

Audit reports do include standard language stating that the audit firm is not engaged to conduct an audit or state an opinion, and that the report is for the company's information only. An Agreed Upon Procedure report, which is governed by the Statements on Standards for Attestation Engagements, as issued by the American Institute of Certified Public Accountants, is a more appropriate format and more cost effective for the nature of oversight. This is the format that most accounting firms follow when generating a JTIP final audit report and what has been accepted by JTIP staff. JTIP staff is in the process of updating language in the contract and policy materials to more accurately reflect the actual practice.

In addition to the standard language noted above, the audit reports do note whether the auditors identify any exceptions or findings during the course of their audit. JTIP staff credits its tightened practices and procedures regarding compliance reviews for the consistent "clean" audit reports for JTIP participants.

A detailed invoice is not required because the scope of the audit is provided by JTIP to the participating companies and audit firms in the form of the JTIP Project Closeout Audit Guide.

The standard is that a compliance review is conducted upon receipt of the initial claim for every JTIP project, and that the claim for reimbursement is not processed for payment until JTIP staff has received the compliance review report with no findings. The general practice is that a follow-up compliance review is requested if the compliance officer encountered any compliance issues during the initial compliance review, or if the project involves large numbers of trainees.

The LFC report, on page 31, makes a number of recommendations EDD should adopt.

- Institute state-specific minimum wage and job count requirements to fully access JTIP reimbursement to drive economic development goals for the state.

As discussed above, JTIP has minimum wage requirements as outlined in the table on page 28, "Federal Department of Labor Guidelines for Wages and Training Hours." In addition, JTIP policy outlines minimum wage requirements for contract-based call centers. For those companies, the wages must meet or exceed at least 90% of the county median wage to qualify in urban locations and pay at least $10.00 per hour in rural locations in order to qualify for JTIP.

The JTIP staff and board would be open to suggestions as to how to implement such state-specific minimum wage and job count requirements without excluding small businesses in both urban and rural

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locations from participation in the program. While the large JTIP projects with well-known corporations are most visible and receive the most public attention, the majority of companies awarded JTIP funds are small businesses that couldn't survive if forced to raise wages or hire beyond their ability of sustaining the business. Nor would traditional manufacturing companies have the resources to pay a minimum of $19.08 per hour as cited in the example on page 27, even in an urban setting.

- Specify in the JTIP compliance officer's professional services contract a scope of work and performance measures

I agree that the scope of work and performance measures in the compliance officer's professional services contract could be more specific, and I will have the JTIP staff outline those items more thoroughly in the future.

- Require JTIP recipient companies to report on job retention and wages for a period of time after final reimbursement for longitudinal analysis, such as three to five years.

JTIP staff currently conducts an annual retention study and could request that companies report on job retention and wages going back further than one year. Once the contract period has ended, the company is not obligated to respond, nor does JTIP staff have the authority to require it, however. Response is voluntary. JTIP agreements could be revised to require participation, and I will ask the JTIP staff to propose this change to the Board.

- Revise JTIP training hour calculations to consider previous work experience, similar to federal Workforce Investment Act requirements.

On page 26, the LFC report states that JTIP funds new employee training without taking previous experience into account. JTIP is an incentive, which provides a monetary value to eligible companies which create jobs in New Mexico. The incentive offsets the cost of lost productivity experienced by a company when ramping up and training its newly-hired employees. While it would be interesting to gauge skill levels before and after JTIP training, the JTIP staff, which consists of three full-time equivalent positions, does not have the time, expertise, or funds to test the skill level of every JTIP trainee prior to being hired by participating companies. Nor does EDD wish to be involved in employment decisions made by participating companies. The EDD trusts that participating companies have HR staffs with ample experience to make employment decisions, based on their own corporate values and educational/skill requirements that are best suited for their company.

EDD understands that every new hire requires training, regardless of their prior education/experience. JTIP is not a "pre-employment" program, however. The LFC report compares JTIP to the Workforce Investment Act Program, whose mission is to improve employee skill levels for access to employment opportunities. To the contrary, EDD's mission is to create an attractive business environment to draw industries which create those jobs.

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- Revise the JTIP contract with recipients to establish what is required from the independently-contracted audit.

I agree that the contract language regarding the independently-contracted audit requires revisions to better reflect the current practice, and will ask JTIP staff to do so.

LEDA Grant Agreements

EDD uses LEDA capital outlay grants to fund two general categories of projects: infrastructure projects and economic development projects. Although no bright line divides these categories and they overlap to some degree, it is a useful dichotomy for analyzing LEDA projects.

Generally speaking, infrastructure projects benefit an entire community or region, providing basic services to the general population. Examples of an infrastructure project include water, sewer, and wastewater systems, such as LEDA funded in Santa Teresa, roads, bridges, and other large-scale developments. Examples of economic development projects include land or a building built for a specific company and for a specific purpose.

Despite the differences between the two categories of projects, both infrastructure and economic development projects build what EDD refers to as the state's community development capacity. Generally speaking, that concept comprises everything necessary to sustain and expand the state's economic base. Capacity building is a conceptual approach to development that focuses on understanding the obstacles that inhibit realization of a community's developmental goals. To build capacity is to enhance the abilities that will allow communities to achieve measurable and sustainable results.

Neither infrastructure nor economic development projects allow for meaningful clawbacks in the way that the LFC report envisions them. The notion that we can simply get back money designated for a project misunderstands the entire LEDA process. EDD cannot and does not write checks to a company. When state LEDA capital outlay funds are used to fund a project, EDD must first approve the scope of work to be performed. The local government pays the contractor that performs that work and then invoices the state. EDD uses the state's LEDA capital outlay funds to reimburse the local government for work that has already been performed. In this context, the LFC report begs an obvious question: from whom would EDD claw money back? The local government has spent the state funds on the project, as was intended. The contractor has performed and is entitled to payment for its work. The project was constructed to the benefit of the community and its local government according to their LEDA ordinance.

On this point, the LFC report states at page 21 that "Intergovernmental Agreements do not include clawback provisions, keeping the state from recuperating [sic] any LEDA capital outlay funds if a company closes or reduces its workforce." That statement exemplifies the misunderstanding of the LEDA proces. For both infrastructure and economic development projects, EDD grants funds to a local government, not the company. EDD's contractual relationship is with the local government, not the company. When a qualifying entity receives the benefit of a LEDA capital outlay grant, the state

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used LEDA capital outlay funds to reimburse a city or county, which acquires land, a building, or infrastructure. The private company then leases the land or the building, or uses the infrastructure to open a new facility or expand an existing one. The IGA is an agreement between EDD and the local government—an intergovernmental agreement. Why would the state recoup funds from a city or county if a private company closes or reduces its workforce? The city or county has done nothing wrong. The company agreed to create the jobs. Only the target company is a legitimate subject of a clawback. Obviously, what is meant here is that the state should recoup its funds from the company. If that is the case, the clawback would not be in the IGA—an agreement between the state and the city or county to which the company is not a party.

More importantly, if economic development funds are used to fund large-scale, large-impact projects that build capacity, the state does not benefit from clawing those funds back. The project will benefit the target company or industry, but it will benefit the state as a whole as well. Whether or not the target company utilizes the project, the project is and remains useful. That community has more capacity. It is better positioned to recruit new businesses and retain existing ones. The state's investment has worth even if the tenant abandons it or goes out of business altogether. By structuring the relationship in a way that meaningfully protects the State's investment, EDD obviates the need for clawbacks to some degree. Moreover, because state funds go to the local government, if the state were to attempt to recover the state funds expended on the project in the event of a default, it would be in the position of attempting to collect from a local government that cannot afford to construct its own water or sewer infrastructure, for example.

The funding mechanism for LEDA capital outlay grants also deserves discussion. Generally, the legislature has appropriated funds to EDD to use to fund LEDA projects pursuant to the statute. Several high-profile projects were funded with special appropriations specifically for those projects, however. Schott Solar, Hewlett Packard, Fidelity, and Santa Fe Studios each received millions of dollars in special appropriations that were specifically designated for those projects, circumventing EDD's usual process for vetting LEDA projects. The LFC report asserts that EDD received $63.6 million in capital outlay appropriations for LEDA projects between 2007 and 2011. Of that amount, $37.9 million—59.6% of legislature's appropriations to EDD for LEDA projects—were special appropriations to those four projects.

Of the remaining $25.7 million appropriated for LEDA projects, all but $2,550,000 went to projects outside of Albuquerque, Rio Rancho, Las Cruces, and Santa Fe. In other words, 90.1% of LEDA capital outlay funds appropriated to EDD and committed to a project through EDD's vetting process went to projects in rural areas. Eighteen of twenty-five projects located in rural areas, and eleven of those rural projects were infrastructure projects.

EDD wholeheartedly agrees that a more comprehensive and accurate mechanism for tracking and evaluating the return on the state's capital outlay investments should be implemented. On page 17, the LFC report recommends that EDD require companies entering into LEDA agreements and JTIP contracts to provide to EDD the quarterly job wage and contribution reports submitted to the New Mexico Department of Workforce Solutions. EDD agrees that this would be an informative reporting

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requirement, and will implement it in future LEDA and JTIP agreements.

Schott Solar

For good reason, the LFC report makes special mention of the Schott Solar deal. In 2008, the legislature appropriated $7.5 million from the General Fund to EDD specifically for the Schott Solar project and $7 million from the General Fund to EDD for LEDA capital outlay grants, of which $500,000 went to the Schott Solar project. In 2009, the legislature appropriated $6 million from Severance Tax Bonds to DFA specifically for the Schott Solar project. Of the $15.9 million that went to the Schott Solar project, only $500,000 went through EDD's vetting process. By appropriating funds directly to the project, the legislature bypassed the procedural safeguards that EDD had in place. The LFC report highlights the absence of clawbacks in the LEDA agreements. KOB TV reported on June 29 that it had obtained a document that read, "the State of New Mexico specifically requested that no performance claw backs be tied to their contribution." Clearly, there were no policies or procedures EDD could have implemented that would have averted this disaster. Even those policies and procedures in place at the time were ignored.

Hewlett Packard

The LFC report also individually addresses Hewlett Packard. On page 22, the report states, "the LFC estimates $238,000 in penalties could be returned to the state if a clawback provision was in place for its contribution." In fact, clawback provisions are in place for both the LEDA capital outlay grant and JTIP funds dedicated to the project, and EDD is in the process of recovering the portion of the state's funds subject to those clawbacks. My staff has already met with HP, at its invitation, to discuss the amounts and timing of those payments. It is also important to note that HP is not going out of business. It is a Fortune 10 company. Its layoffs in Rio Rancho were a part of its global restructuring. It is going to repay what it owes to the state and continue in business. Moreover, the LFC report acknowledges that HP has already injected $196 million into the state's economy in payroll alone. The LFC should recognize that return on the state's investment.

Santa Fe Studios

Page 23 of the LFC report states, "[t]he Santa Fe Studios $28 million project could prove to be a risky investment to the state with its $10 million contribution." EDD, the entire Martinez administration, and I could not agree more. The legislature chose to appropriate funds directly to that project, however, circumventing EDD's process for financially vetting LEDA projects. The report further asserts that "[a]ll construction jobs are to be credited towards [sic] the job hour requirements." That is incorrect. As the LEDA documents the LFC's staff reviewed make clear, construction jobs do not count toward Santa Fe Studios' job creation requirements. In fact, construction jobs never count toward the job creation requirements for LEDA projects.

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Conclusion

As I have told committee members throughout my tenure, EDD is more than willing to participate in a meaningful assessment of tax expenditures and incentives. I believe that evaluation would be of great benefit to the taxpayers. EDD must have access to the information and resources necessary to perform that assessment, however. The analysis must also take into account all relevant information—the state's systemic need for incentives in order to compete, the benefits of incentives as well as their costs, and the limitations on economic development efforts. I look forward to continuing to work with you to achieve these goals create a better environment for economic development.

Sincerely,

Jonathan L. Barela
Cabinet Secretary
New Mexico Economic Development Department

cc: LFC Members

The Taxation and Revenue Department did not provide a response to the evaluation.

APPENDIX A: Evaluation Objectives, Scope and Methodology

Evaluation Objectives.

- Review the administration and oversight of JTIP and projects authorized under LEDA.
- Assess the cost and outcomes produced by JTIP and projects authorized under LEDA.
- Review best practices in economic development incentive performance measurement and compare to current state practices.

Scope and Methodology.

- Reviewed state statutes, departmental, and division policies, procedures, and internal management documents.
- Conducted structured interviews with Economic Development Department and Taxation and Revenue Department agency staff, county and municipal economic development staff, economic developers, other state economic development and legislative audit staff, and JTIP and LEDA recipients.
- Reviewed financial, performance, and quality data from the department.
- Reviewed published literature on other state practices, press releases, and media reports relevant to the evaluation.
- Site visits for two LEDA recipients.

Evaluation Team.
Charles Sallee, Deputy Director
Maria D. Griego, Lead Program Evaluator
Brenda Fresquez, Program Evaluator

Authority for Evaluation. The LFC is authorized under the provisions of Section 2-5-3 NMSA 1978 to examine laws governing the finances and operations of departments, agencies, and institutions of New Mexico and all of its political subdivisions; the effects of laws on the proper functioning of these governmental units; and the policies and costs. The LFC is also authorized to make recommendations for change to the Legislature. In furtherance of its statutory responsibility, the LFC may conduct inquiries into specific transactions affecting the operating policies and cost of governmental units and their compliance with state laws.

Exit Conferences. Status meetings were held with the Economic Development Department on July 31, 2012, and with the Taxation and Revenue Department on August 3, 2012. A report draft was provided to both agencies on August 10, 2012 for comment. The contents of this report were discussed with the Economic Development Department and the Taxation and Revenue Department during the exit conference on August 15, 2012.

Report Distribution. This report is intended for the information of the Office of the Governor, the Economic Development Department, the Taxation and Revenue Department, Office of the State Auditor, and the Legislative Finance Committee. This restriction is not intended to limit distribution of this report, which is a matter of public record.

Charles Sallee
Deputy Director for Program Evaluation

APPENDIX B: Estimated Cost per Job Analysis – Sample of JTIP Recipients FY07-FY11

Company	Location	JTIP Funded Positions	JTIP Funds Expended	JTIP Average Cost per Job	Average Wage	Average Annual Salary	*Estimated High Wage Job Credit (for max of 4 qualifying periods total)*	*Estimated Rural Job Tax Credit (for max qualifying periods)*	*Estimated LEDA Average Cost per Job Using Projected # of Jobs*	*EstimatedLEDA A Average Cost per Job Annualized Weighted*	*Estimated Average Total Cost per Position with LEDA Projected Jobs Calc*	*Estimated Average Total Cost per Position with LEDA Annualized Weighted Calc*
C/D Squared Enterprise	Gallup	1	$11,330	$11,330	$14.21	$29,557	*$11,823*	*$2,000*	*$0.00*	*$0.00*	*$25,153*	*$25,153*
CFV Solar Test Laboratory, Inc.	Albuquerque	6	$68,715	$11,246	$24.88	$51,750	*$47,101*	*$0.00*	*$15,000*	*$750*	*$49,797*	*$35,547*
Fidelity Employer Services Company LLC	Albuquerque	281	$1,212,285	$4,305	$16.54	$34,396	*$53,658*	*$0.00*	*$11,111*	*$9,251*	*$33,302*	*$31,442*
Hewlett-Packard	Rio Rancho	683	$7,436,473	$9,714	$23.88	$49,678	*$206,661*	*$0.00*	*$8,889*	*$2,370*	*$44,435*	*$37,916*
Louisiana Energy Services	Eunice	15	$282,662	$18,962	$39.21	$81,557	*$84,819*	*$8,000*	*$2,778*	*$0.00*	*$68,150*	*$65,372*
PreCheck, Inc.	Alamogordo	47	$309,421	$6,437	$12.28	$25,542	*$0.00*	*$6,000*	*$0.00*	*$0.00*	*$8,437*	*$8,437*
Schott Solar, Inc.	Albuquerque	162	$1,458,233	$7,860	$19.48	$40,518	*$47,947*	*$0.00*	*$21,687*	*$13,012*	*$41,534*	*$32,859*
Outcomes	Albuquerque	36	$258,648	$7,185	$27.16	$56,493	*$29,376*	*$0.00*	*$0.00*	*$0.00*	*$36,561*	*$36,561*
Tempur Production USA	Albuquerque	11	$108,948	$9,904	$14.58	$30,326	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$9,904*	*$9,904*
PolyFlow Engineering	Albuquerque	7	$45,770	$6,539	$20.95	$43,576	*$22,660*	*$0.00*	*$0.00*	*$0.00*	*$29,198*	*$29,198*
Lovelace Respiratory Research Institute	Albuquerque	30	$130,306	$4,465	$19.12	$39,777	*$43,459*	*$0.00*	*$0.00*	*$0.00*	*$18,951*	*$18,951*
Results, Las Vegas, NM	Las Vegas	96	$295,532	$3,078	$9.14	$19,011	*$0.00*	*$4,000*	*$0.00*	*$0.00*	*$7,078*	*$7,078*
Southwest Cheese	Clovis	28	$108,694	$3,882	$14.50	$30,160	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$3,882*	*$3,882*
AerSale	Roswell	31	$107,782	$3,477	$15.07	$31,346	*$16,300*	*$2,000*	*$0.00*	*$0.00*	*$21,777*	*$21,777*
General Mills	Albuquerque	52	$136,034	$2,616	$13.50	$28,080	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$2,616*	*$2,616*
CVI, Laser	Albuquerque	12	$129,520	$14,024	$25.87	$53,817	*$64,204*	*$0.00*	*$0.00*	*$0.00*	*$35,425*	*$35,425*
MIMICS	Albuquerque	4	$41,020	$10,807	$26.11	$54,309	*$84,722*	*$0.00*	*$0.00*	*$0.00*	*$39,047*	*$39,047*
Aero Mechanical	Rio Rancho	33	$214,692	$6,255	$15.80	$32,871	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$6,255*	*$6,255*
Premier Pellets	Tularosa	18	$95,975	$5,332	$12.17	$25,314	*$0.00*	*$4,000*	*$0.00*	*$0.00*	*$9,332*	*$9,332*
Total/Average:		**1,553**	**$12,452,040**	**$8,414**	**$19.18**	**$42,840**	***$712,729***	***$26,000***	***$5,273***	***$2,332***	***$30,867***	***$27,925***

APPENDIX C: Economic Development Department 3rd Quarter Report Card – FY12

Performance Report Card
Economic Development Department
Third Quarter, Fiscal Year 2012

Performance Overview: The Economic Development Department is exceeding the average number of jobs created per quarter necessary to meet the FY12 target, and the department surpassed the rural jobs target. Recent business recruitment and business expansion activity boosted job creation performance outcomes compared to FY11.

Economic Development Program		Budget: $2,887,000	FTE: 26	FY11 Actual	FY12 Target	Q1	Q2	Q3	Q4	Rating
1	Total number of jobs created due to economic development department efforts *			1,922	2,500	282	1,392	538		G
2	Total number of rural jobs created *			958	1,100	230	666	434		G
3	Number of jobs created through business relocations facilitated by the economic development partnership *			499	2,200	0	450	127		R
4	Number of leads created through the economic development partnership			New	400	109	101	74		Y
5	Number of jobs created by the mainstreet program *			598	570	199	97	171		G
6	Percentage of employees whose wages were subsidized by the job training incentive program still employed by the company after one year *			47%	60%	Annual				-
7	Average annual cost per job training incentive program trainee			New	$2,500	$8,783	$6,162	$3,570		Y
Program Rating				Y						G

Comments: The department reports the number of jobs created is based on announced or planned jobs as opposed to actual jobs created in the present sense. A substantial increase in the number of announced new jobs occurred in the second quarter. The department reported 2,216 new jobs in the first three quarters of FY12, which is more than half of the 4,000 net new jobs reported for New Mexico by the U.S. Department of Labor Bureau of Labor Statistics (BLS) from March 2011 to March 2012. New Mexico is ranked 38 of 51 for total employment growth by the BLS. The performance outcomes for the Economic Development Partnership dipped recently due to reduced expansion opportunities, caused by slow economic recovery and business concerns about future economic growth. In addition, the Partnership is now receiving less funding through its contract with the EDD – resulting in fewer out of state travel trade shows attended. The JTIP missed the targeted average cost per job; however, this is a new measure and the target may need to be adjusted upward based on historical averages and efforts to increase the wage base of program participants. The lower cost for the third quarter is mostly due to funding jobs with lower average wages than in the first two quarters. Given a cost per job of tens of thousands of dollars in some other development programs, the JTIP is managing its funds well. One of the incentive programs used by the department, the High-Wage Jobs Tax Credit, has rapidly escalating costs, and new job growth has not increased proportionately to account for the rising costs.

Film Program		Budget: $868,100	FTE: 9	FY11 Actual	FY12 Target	Q1	Q2	Q3	Q4	Rating
8	Number of media industry worker days *			181,366	150,000	41,939	34,437	39,140		G
9	Economic impact of media industry productions in New Mexico, in millions			$696.6	$300	$153.0	$89.0	$224		G
10	Number of films and media projects principally made in New Mexico			96	60	10	10	18		Y
Program Rating				G						G

Comments: The Film Program performance report is focused on reporting output activity such as outreach and workforce development. The quarterly report notes the number of meetings with studio and production entities and planned attendance at trade shows, meetings, and outreach programs with local governments, and number of job training opportunities facilitated through the JTIP. The report provides no narrative on outcome measures such as economic impact to the state, number of film and media projects filmed in New Mexico, etc. However, the Film Office website provides much of this data.

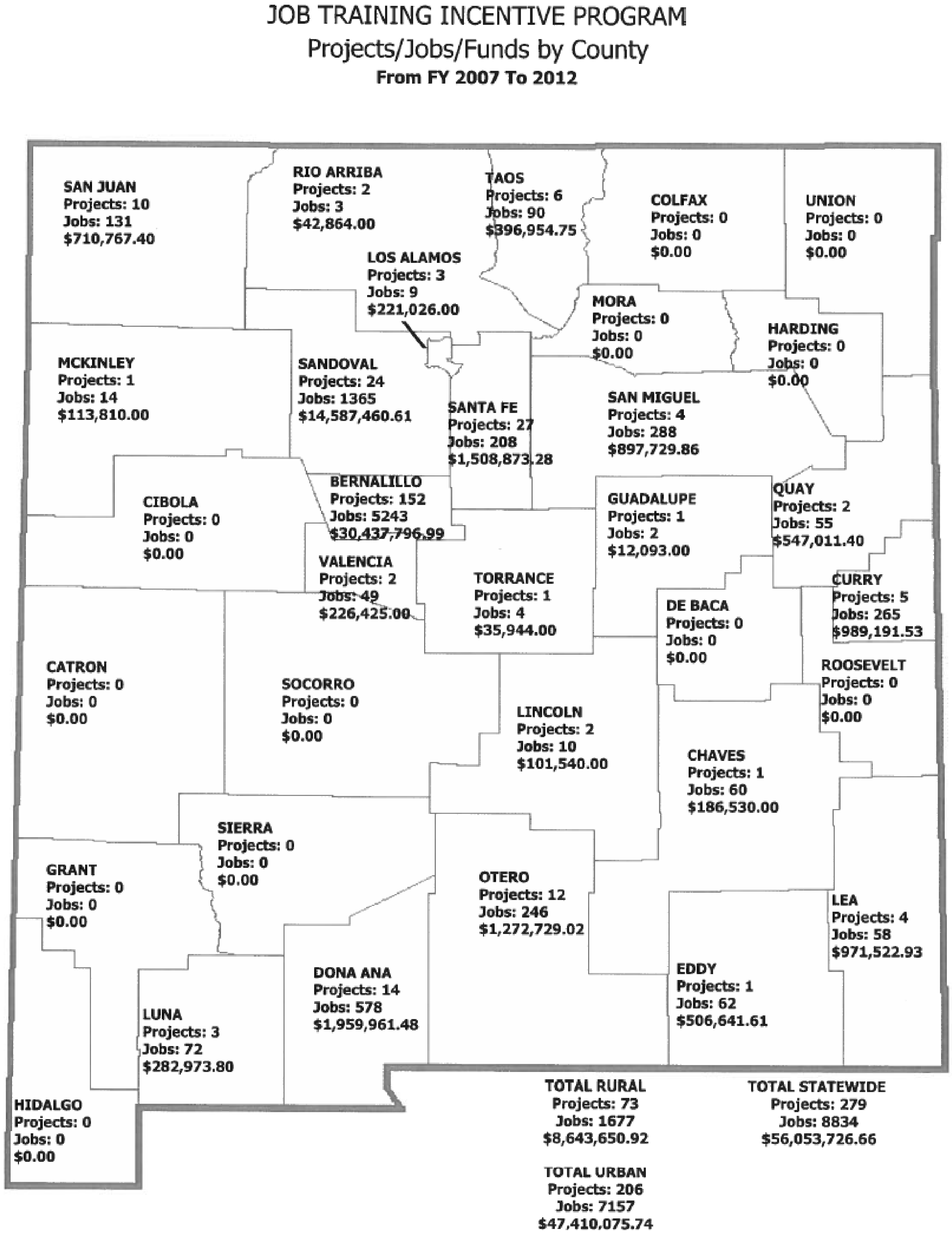
Technology Commercialization Program	Budget: $20,000	FTE: 0	FY11 Actual	FY12 Target	Q1	Q2	Q3	Q4	Rating
11	Amount of investment as a result of office of science and technology efforts, in millions *		$87.6	$30.0	n/a	n/a	n/a		-
Program Rating			G						-

Comments: Without FTE and a reduced operating budget, there is little program activity to report for FY12. The department reports it is identifying how to reactivate the program's functions as part of a restructuring plan.

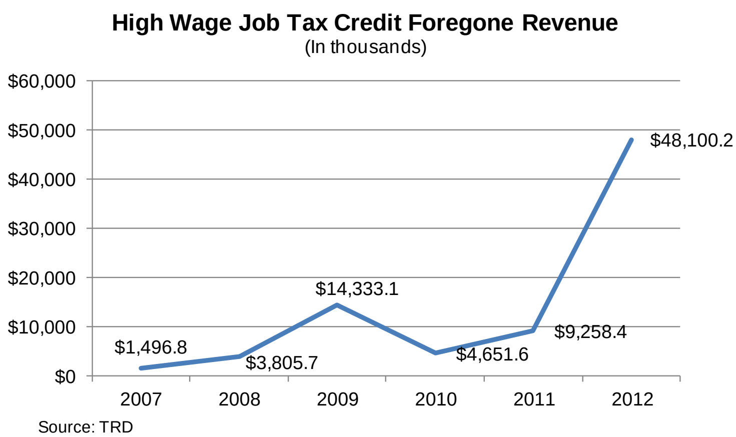
Suggested Performance Measure Improvement

- The Economic Development Department substantially improved its quarterly report to include action plans, goals, objectives, and graphical representations of performance outcomes. Benchmarking is recommended so measures have comparison to other states or national standards.

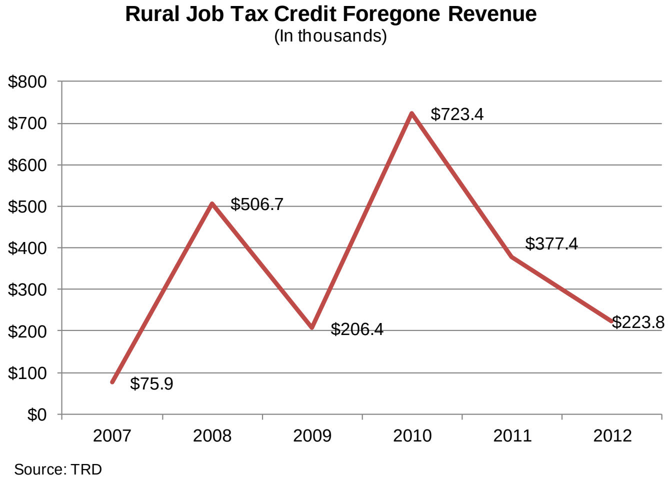
APPENDIX D: JTIP Projects, Jobs and Funds by County



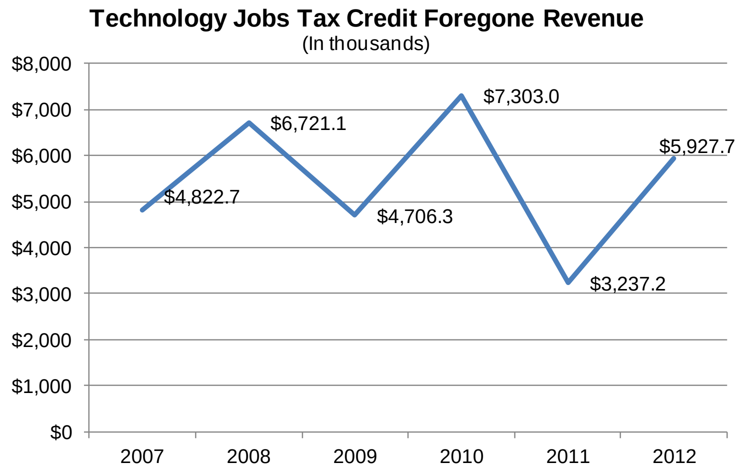
The High Wage Jobs Tax Credit (HWJTC) was created in 2004, with the goal of incentivizing the creation of high wage economic base jobs in New Mexico. The credit is defined as 10 percent of an employee's wages and employer paid benefits up to a maximum of $12 thousand per year. Statute defines a high wage job as having a $40 thousand per year salary in an urban area (over 40 thousand residents), and a $28 thousand per year salary in a rural area (under 40 thousand residents.) The taxpayer may take the credit for a maximum of four years after a one-year qualifying period is met. This is a refundable credit, so if the credit exceeds the filer's tax liability, they will be refunded the excess credit. The taxpayer has to complete a certification process with the TRD to be eligible for the credit, and also submits a form with tax returns detailing the amount of the credit being taken. The EDD is responsible for reporting on the credit to interim committees of the legislature on an annual basis. The last report to LFC was made in November 2011. The credit is currently set to sunset on July 1, 2015. Foregone revenue for FY12 was reported by the TRD as $48.1 million, with an average claim of $17 thousand.



The Rural Job Tax Credit (RJTC) was established in 1999 to spur job growth in rural areas of the state. A rural employer can claim between 12.5 percent and 25 percent of the first $16 thousand of an employee's salary for to be paid out over two to four years based on the size of the rural area in which the business is located. Rural areas are defined as having either more or less than 15 thousand residents, and are located further than 10 miles away from a metropolitan area. Similar to the HWJTC, taxpayers must be certified to be eligible for this credit, must be approved for JTIP, and can apply for the credit after a one year qualifying period. Statute dictates that the TRD, EDD, and WSD must jointly evaluate the effectiveness of the credit in stimulating job growth in rural areas and report their findings to the Legislature. There is not a sunset provision for this credit. Foregone revenue for FY12 was reported by the TRD as $224 thousand.

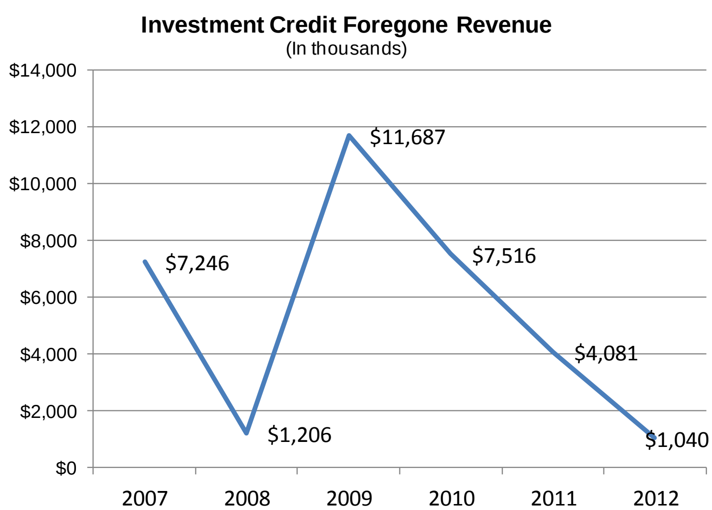


The Technology Jobs Tax Credit was created in 2000 to provide a favorable tax climate for technology-based businesses engaging in research, development and experimentation and to promote increased employment and higher wages in those fields in New Mexico. The credit allows a qualified technology-based research facility that is not government-affiliated to claim a four percent credit against expenditures made in the research process including land, improvements, equipment, and payroll among others. An additional four percent can be claimed if the taxpayer increases payroll by $75 thousand per year, and also requires an additional payroll increase of the same amount for every $1 million in expenditures reported to claim the credit. If the facility is located in a rural area, the credit doubles to 8 percent, with an option for an additional 8 percent if the taxpayer meets the payroll requirement. The TRD has to approve taxpayers to claim this credit, after a one-year qualifying period has passed. The amount of the credit claimed cannot exceed the taxpayer's personal or corporate income tax, but can be carried forward to subsequent tax years. This credit does include a clawback provision if the company ceases operations for 180 consecutive days within a two-year period, where all unclaimed credit is voided and all taxes for which the credit was taken must be paid. The TRD is required to report on this credit to the LFC on an annual basis assessing fiscal and economic impact, including number of claimants and credits taken, geographic location of taxpayers, and payroll increases noted, all subject to confidentiality provisions. Foregone revenue for FY12 was reported by the TRD as $5.9 million, with an average claim of $25 thousand.



Source: TRD

The Investment Credit was established in 1979 with the purpose of providing a favorable tax climate for manufacturing businesses and to promote increased employment in New Mexico. The credit can be taken as the percentage of the compensating tax rate applied to the value of qualified equipment claimed by a taxpayer conducting manufacturing in the state. The equipment must be owned or leased by the taxpayer, and must be brought into the manufacturing process within one year. Additionally, to claim this credit the taxpayer must increase employment by one person every year for every $500 thousand credit claimed up to an equipment value of $30 million, and for every $1 million credit claimed for over $30 million in equipment. In FY2021, this employment stipulation will be required for every $100 thousand in claimed credit. Statute prescribed a review in the interim of 2005, but there is no stipulation requiring this credit be reviewed regularly by the TRD to inform the Legislature. Foregone revenue for FY12 was reported by the TRD as $1 million, with an average claim of $16 thousand.



Source: TRD

The Research and Development Small Business Tax Credit was created in 2005. This credit allows the taxpayer to claim a credit equal to the sum of all gross receipt taxes or 50 percent of withholding taxes for conducting technological research to develop or improve a business product. A business qualifies for the credit if the business has less than 25 full-time employees, has total revenues that are less than $5 million, and does not have 50 percent of its voting stock owned by another business. Also stipulated in the statute is that any business claiming this credit is ineligible the Capital Equipment Tax Credit, the Investment Tax Credit, or the Technology Jobs Tax Credit. There is no legislative reporting requirement for the credit. This credit had a blackout period for FY10 and FY11. In FY09, foregone revenue for the Research and Development Small Business Tax Credit was $108 thousand, with an average credit of $1,600 according to the TRD.