F I S C A L   I M P A C T   R E P O R T

SPONSOR Sapien

ORIGINAL DATE 02/12/13
LAST UPDATED

HB

SHORT TITLE Product Manufacture Reinvestment Tax Credit

SB 236

ANALYST van Moorsel

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY13	**FY14**	**FY15**	**FY16**	**FY17**		
	($9,900.0)	($11,700.0)	($14,040.0)	($15,300.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

Relates to SB 13, SB 59, SB 277, HB 182/HTRCS

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)

SUMMARY

Synopsis of Bill

Senate Bill 236 (SB 236) creates a new section of the Corporate Income and Franchise Tax Act to create a new credit against a taxpayer's corporate income tax (CIT) liability. This "manufacturing consumption tax credit" may be claimed for up to 60 percent of the amount paid on consumables purchased in the taxable year and consumed in the manufacturing process.

The bill provides that to be eligible for the credit, the taxpayer must invest in capital equipment or facilities construction or renovation in New Mexico on or after January 1, 2013 and prior to January 1, 2021.

The Economic Development Department (EDD) may find a taxpayer eligible for the credit for the following terms based on the following amounts of investment in a taxable year:

- four consecutive years if the taxpayer invests at least $200 million;
- three consecutive years if the taxpayer invests between $100 million and $200 million;

- two consecutive years if the taxpayer invests between $50 million dollars and $100 million; and
- one year if the taxpayer invests at least $10 million but less than $50 million.

The taxpayer may claim only one tax credit at a time, and may carry forward any credit amount in excess of the taxpayer's liability for four years, provided that the carry forward may not be applied during the term of a taxpayer's manufacturing consumption tax credit. The bill provides that the taxpayer may not claim other credits for the same investment pursuant to the Corporate Income and Franchise Tax Act, the Gross Receipts and Compensating Tax Act or the Investment Credit Act or for credits that may be taken against the taxpayer's modified combined tax liability

There is no effective date of this bill. It is assumed that the new effective date is 90 days after this session ends (June 14, 2013). The provisions of the bill apply to taxable years beginning on or after January 1, 2013.

FISCAL IMPLICATIONS

In its analysis if SB 236, the Taxation and Revenue Department (TRD) cites 2010 New Mexico CIT data from the manufacturing sector in reporting that about 210 taxpayers had taxable income greater than $30 million ($10,000,000 × 3, assuming that 1/3 of the taxable income would be the qualified investment amount). Of these taxpayers, only 21 taxpayers paid taxes greater than $180 thousand ($10,000,000 × 30 percent × 6 percent, assuming that 30 percent of the investment would be purchased in qualified consumable tangible properties). Thus, the TRD estimates 19 firms would claim this credit in FY14. The TRD details its estimate in the following table.

Type of Investment	Number of Investments	Eligibility Period	Purchases of Consumable Tangible Property % of Total Investment
Annual investment ≥ 200 million	1	4 years	30%
Annual investment ≥ 100 million	1	3 years	30%
Annual investment ≥ 50 million	2	2 years	30%
Annual investment ≥ 10 million	15	1 year	30%

The TRD's analysis assumes that these qualified firms would invest the qualified amount again to be eligible for another new period at the end of the period of the initial credit. The analysis also assumes some new firms would be attracted to invest more due to the availability of this credit.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations.

Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

SIGNIFICANT ISSUES

SB 236 states the purpose of the manufacturing consumption tax credit is to provide manufacturers in the state with an incentive that decreases the cost of production and promotes longevity, increased employment, retention and expansion of manufacturing businesses.

New Mexico's top corporate income tax rate of 7.6 percent is high, compared with the national average of 6.4 percent. New Mexico's CIT rate is especially high when considering a corporation can be taxed at the 4.9 percent personal income tax rate simply by organizing under another section of the IRS code. This violates the principle of tax equity. In 2011, the Council on State Taxation (COST) commissioned Ernst & Young to perform a 50-state study of effective tax rate/after-tax return on investment over a 30-year investment, New Mexico ranked last. The study found that tax rates and a complex tax credit incentive system are a burden on firms considering investments in New Mexico and are "almost certainly impeding economic growth." Among other options, the New Mexico Tax Research Institute (NMTRI) noted a reduction in the top CIT rate would make New Mexico more appealing to investment (see "Alternatives").

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill's requirement that the TRD compile an annual report that includes the number of taxpayers approved by the TRD to receive a manufacturing consumption tax credit and the total amount of credits authorized. The bill further provides that acceptance by a taxpayer of a manufacturing consumption tax credit is authorization by the taxpayer receiving the credit for the TRD to reveal information to the Legislature necessary to analyze the effectiveness of the credit.

CONFLICT, DUPLICATION, COMPANIONSHIP, RELATIONSHIP

Relates to SB 13 - Corporate Income Tax Rates and Reporting; SB 59 – Corp. Tax Reporting, Single Sales & Repeals SB 277 – Single Sales & Reduce Corporate Sales Tax**;** HB 182/HTRCS – Single Sales & Reduce Corporate Sales Tax.

ALTERNATIVES

Several pieces of legislation introduced during the 2013 legislative session would reduce the CIT rate. Volume I of the "Report of the Legislative Finance Committee to the Fifty-First Legislature, First Session" states that one area of tax policy warranting policy changes includes reduction of tax rates and concurrent broadening of the corporate income tax base. SB 236 would make the tax base narrower, and an alternative would be a broader CIT base at a lower rate.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

PvM/svb