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FISCAL IMPACT REPORT

		LAST UPDATED	
SPONSOR	Griggs	**ORIGINAL DATE**	1/19/2024
SHORT TITLE	Mall Renovation Tax Credit	**BILL NUMBER**	Senate Bill 22
		ANALYST	Gray

REVENUE*
(dollars in thousands)

Type	FY24	FY25	FY26	FY27	FY28	Recurring or Nonrecurring	Fund Affected
PIT/CIT		Up to ($100,000.0)	Up to ($100,000.0)	Up to ($100,000.0)	Up to ($100,000.0)	Recurring	General Fund

Parentheses ( ) indicate revenue decreases.
*Amounts reflect most recent analysis of this legislation.

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT*
(dollars in thousands)

Agency/Program	FY24	FY25	FY26	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
TRD – RPD, ASD, ITD		$12.5		$12.5	Nonrecurring	General Fund

Parentheses ( ) indicate expenditure decreases.
*Amounts reflect most recent analysis of this legislation.

Sources of Information

LFC Files

Agency Analysis Received From
Taxation and Revenue Department (TRD)
Economic Development Department (EDD)

SUMMARY

Synopsis of Senate Bill 22

Senate Bill 22 creates a personal and corporate income tax credit for real estate property owners renovating their properties. The owners of malls, shopping centers, and other large retail developments are eligible for the credit if those properties provide commercial space to 20 or more retail, food, or beverage businesses.

The contemplated credit would be equivalent to the gross receipts taxes paid on the construction activity for restoration, renovation, and rehabilitation projects. The credit expires after 10 years.

These credits have a cap of $50 million for PIT and $50 million for CIT, for a cumulative of $100 million.

This bill does not contain an effective date and, as a result, would go into effect 90 days after the Legislature adjourns, or May 15, 2024, if enacted. The provisions of the act apply to taxable years beginning on or after January 1, 2024.

FISCAL IMPLICATIONS

This bill creates a tax expenditure. 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.

LFC has serious concerns about the substantial risk to state revenues from tax expenditures and the increase in revenue volatility from erosion of the revenue base. The committee recommends the bill adhere to the LFC tax expenditure policy principles for vetting, targeting, and reporting or action be postponed until the implications can be more fully studied.

The credit created by SB22 intends to offset the GRT cost of renovations for some real estate property owners, subsidizing those costs from between 6 percent and 8 percent, depending on the location of the project. Many unknown factors could impact the total cost to the state and total costs may be significant. Neither TRD nor LFC analysis provides a point estimate; because of credit caps, costs cannot exceed $100 million.

SIGNIFICANT ISSUES

Highly targeted tax policy like that contemplated in SB22 results in some businesses becoming stronger while others become weaker. The credit may create negative incentives, distort market dynamics, and generate unknown impacts.

The credit does not meet standard economic development objectives. It likely does not pass the "but for" test, which asks whether an incentive encourages some economic activity that would not have occurred "but for" the incentive. Renovations are a fundamental operating expense for any property and those renovations must be completed for the continued operation of a facility. Therefore, the credit does not encourage activity that would not have occurred but for the incentive. The credit may prevent property owners from becoming delinquent, but subsidies do not fix the underlying cause of such delinquency, such as revenue problems. If the credit does prevent a property from becoming delinquent, the property will still become delinquent when the credit expires unless the state agrees to permanently offset those costs.

The credit likely will negatively impact the competitiveness of smaller property owners. Small real estate property owners that do not operate malls or other shopping centers will face a competitive disadvantage relative to their larger peers. The long-term negative consequences are unknown but may be significant for a community, especially because renovation costs make up a relatively large portion of on-going operational expenses.

Lastly, the retail operations in malls, shopping centers, or large retail developments are not part of the state's economic base. Incentives should target economic base industries because they help bring in new dollars from outside the state. Non-economic base industries—like retail, food, and

beverage businesses—do not increase the overall wealth and well-being of New Mexicans.
TRD recommends the proposal be a GRT deduction rather than a PIT or CIT credit.

> Deductions are simply claimed on GRT returns by taxpayers, and TRD simply processes them. This is much more straightforward than the proposal in this bill. Here, taxpayers would be required to pay GRT regularly, and then submit a credit application to EDD; EDD would review and certify the credit; and finally, the taxpayer would claim the credit on an annual PIT or CIT return from TRD. TRD would have to track carryforward of unused credits for 5 years.

TRD also notes that a taxpayer may not receive the benefit of the entire credit because it is non-refundable. They note that during a large renovation project, a mall "may have negative taxable income and net operating losses that reduce or eliminate their tax liability, causing the incentive to go unused." Some—but not all—of this issue is resolved because the credit may be carried forward for up to five years.

TECHNICAL ISSUES

The bill defines a mall as "real property" that "provides space for at least twenty individual businesses that provide retail or food or beverage establishments." Real property is defined as a parcel of land and everything permanently attached to the land, like buildings. Therefore, a large shopping center with 20 or more retail, food, or beverage businesses would be considered a mall under this definition. Such large shopping centers are often owned by developers and leased to businesses. It is unclear whether these areas were intended to be included by SB22 because they are not generally referred to as "malls." Further, large shopping centers may have significantly higher renovation costs than what would traditionally be thought of as a "mall."

TRD provides various technical issues.

> On page 2 and page 5, under Subsection B., the credit depends on the GRT rate, which may change semi-annually on January 1 and July 1. The bill should specify which rate be used when calculating the credit. TRD suggest the following language: "the rate that is effect when the expenses were incurred."
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> For clarity purposes, TRD recommends a change in the language in Page 2, line 12-14. Such language might read: "plan, including phases of construction, if any. If the economic development department determines that the mall renovation project is likely to meet the requirements for mall renovation income tax credit,". The same recommendation is made in Page 6, lines 8-10: "plan, including phases of construction, if any. If the economic development department determines that the mall renovation project is likely to meet the requirements for mall renovation corporate income tax credit,".
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> There is a time limit for when a taxpayer must apply for the certification of the credit from the EDD, but there is no limit on when the taxpayer must claim the credit on a tax return. Adding a deadline to claim the credit will help keep the $50 million certification cap for both PIT and CIT claimed consistent over each tax year. TRD suggests adding language at page 3, line 10, stating that the tax credit must be claimed starting in the year that the credit is certified as eligible by EDD. TRD suggests the following language: "A taxpayer who receives a certificate of eligibility shall claim the

credit commencing in the first eligible tax year stated in the certificate of eligibility." On page 2, lines 19-20, the taxpayer is required to apply within one calendar year of "completion" of the project. It is not clear when a project is completed, or who makes that determination. TRD recommends the following language: "Within one calendar year of the date that the project manager of a mall renovation project or owner of the mall certifies that the mall renovation project is complete…"

On page 3, line 2, and page 6, line 23, applications for certification of the credit will not be approved if EDD has already approved $50 million in certifications in that calendar year. But this only affects the approval process; it fails to limit what may be paid out in any given fiscal year because the credit can be carried forward to future tax years. More certainty, control, and accountability could be achieved through an amendment reflecting language found in Section 7-2-18.32(D) NMSA 1978.

TRD recommends the following additions on page 3, line 9 and page 7, line 5, after "approved.": "The certification must include the taxpayer identification number, first eligible tax year, and shall be numbered for identification and declare its date of issuance and the amount of the tax credit allowed. The economic development department shall provide the taxation and revenue department appropriate information for all eligible taxpayers to whom certificates are issued. The method of interagency certification sharing shall be in secure and performed on regular intervals agreed upon by both the taxation and revenue department and the economic development department."

These credits are separate under Income Tax and Corporate Income Tax acts. However, it is unclear whether EDD must be able to determine which tax credit the taxpayer is eligible for or intends to take. TRD suggests an aggregate certification cap across both the Income Tax and Corporate Income Tax acts to remove any responsibility for EDD to predetermine which type of credit will be claimed. TRD suggests in Section 1, subsection D. and Section 2, subsection D., after the "aggregate amount of credits" add, "combined for Mall Renovation income tax credits and corporate income tax credits."

The bill does not state that a taxpayer that claims a mall renovation income tax credit pursuant to the Income Tax Act shall not also claim a mall renovation corporate income tax credit pursuant to the Corporate Income Tax Act for the same renovation project. TRD suggests in Section 1, subsection D. and Section 2, subsection D., that the language specify one credit certification per project. Such language might read: "A taxpayer that has submitted an application for a mall renovation corporate income tax credit with respect to a mall renovation project may not submit an application for a mall income tax credit with respect to the same mall renovation project" for Section 1, Subsection D, and "A taxpayer that has submitted an application for a mall renovation income tax credit with respect to a mall renovation project may not submit an application for a mall renovation corporate income tax credit with respect to the same mall renovation project" for Section 2, subsection D.

In Section 1, page 4, line 24 and Section 2, page 8, Line 7, the definition of "qualifying costs" states that the taxpayer has not received a federal credit for the federal new markets tax credit. The bill does not detail what information will be provided to EDD

to verify this condition in determining final qualifying costs and therefore the amount of the credit.

Page 3, line 9 does not establish whether the taxpayer can appeal or protest a denied application.
On page 4, lines 16-19, the definition of "mall" is problematic. In the first instance, it is not the mall itself that provides space to the businesses, but rather the owner of the real property constituting the mall that does so. Second, the words "provides space" are ambiguous and not capable of being evenly applied. This term might include real property that is provided free of charge, or where a business is simply allowed to occupy space. Finally, the language "individual businesses that provide retail or food and beverage establishments" is confusing. It is not clear when a business is an "individual" business, or how a business provides an "establishment", or how an "establishment" differs from a "business". TRD suggests the following alternative language: "'Mall' means real property located in New Mexico whose owners have leased or licensed retail space within or on that real property to at least 20 retail or food or beverage businesses."

On page 4, lines 21-22, the term "seventy-five percent of a mall" is unclear. TRD suggests stating instead "seventy-five percent of the overall square footage of a mall, including both indoor and outdoor real property within the exterior boundaries of the mall."

Page 5, line 2, page 8, and line 10 include "construction-related equipment" as a "qualifying cost." However, the bill does not establish if construction-related equipment must be purchased to qualify for the credit or if they can be rented, which is typically the case.

The bill does not state that EDD may create regulations if needed. TRD suggests allowing EDD to develop rules. An example of this language is in Subsection F of Section 7-2-18.19 NMSA 1978, "The energy, minerals, and natural resources department may issue rules governing the procedure for administering the provisions of this subsection."

OTHER SUBSTANTIVE ISSUES

TRD notes:

While the bill requires pre-certification of the costs, it is unclear what purpose pre-certification is meant to serve. Pre-certification does not carry any benefits, nor does failure to get pre- certification carry any penalties. While the bill states that a "taxpayer shall apply for pre-certification", e.g. on p. 2, line 6, it is not clear what the consequences of failure to apply for such pre-certification are. Furthermore, if EDD does not approve a pre-certification application, it is not clear what the consequences of such refusal will be. TRD suggests striking the entirety of Section C of the bill, as it appears to serve no purpose other than adding administrative costs and complexity to the bill.

Section D of the bill requires that the taxpayer obtain an affidavit from a certified public accountant (CPA) “verifying that the qualifying costs were incurred by the taxpayer and meet the requirements of this section.” TRD believes that CPAs will be reluctant to provide this certification, as it goes beyond an accounting function and requires legal analysis. Furthermore, EDD will review the application before certifying and will be making this determination for itself before approving the credit. TRD recommends striking the language on page 2, lines 23-25 adding this requirement.

TRD is now required by Section 7-1-84 NMSA 1978 to compile and present a tax expenditure budget, which includes the number of taxpayers that claim and the amount of claims for a tax expenditure. Credits are seen as a tax expenditure and will be included in this report. For that reason, TRD recommends that on page 4, lines 6 through 14 and page 7, lines 14 through 22 are stricken in full.

The credits’ calendar year cap will be determined by EDD at the time of certification. In a calendar year, the claims made on returns may not match that cap amount. Thus, the amount certified and the amount in credits claimed in a tax year as reported in the tax expenditure report will differ as the two are separate processes. Overall, the aggregate amount claimed should not exceed the aggregated cap amounts.

A memorandum of understanding will be required to ensure certification data from EDD is shared with TRD if not required statutorily.

BG/rl/ne