

High-Wage Jobs Tax Credit Issues

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Background:

The High-Wage Jobs Tax Credit is one of the most important tools in the State's economic development efforts. The 2010 study of New Mexico's competitiveness by Ernst & Young found that NM went from an effective tax rate double the average in the region to one below average after applying incentives. Wage subsidies like the HWJTC were one of the most important incentives in their analysis. A number of issues have arisen in recent years that suggest the need for structural reform of the credit. The goals of such reform efforts should be to improve the targeting of the credit, improve its predictability in terms of the fiscal impacts and strengthen its effectiveness as an economic development tool.

Statutory provisions:

A refundable credit is allowed equal to 10% of the value of wages and benefits for a four-year period for each new job created with wages of at least \$40,000 in larger municipalities¹ and \$28,000 elsewhere. The job must be with an employer who made 50% of their sales to persons outside New Mexico or who was eligible for JTIP. There is a maximum of \$12,000 per year on the amount of credit per job.

Issues for consideration:

1. Fiscal Impacts:

TRD data indicate a sharp increase in credit claims in FY12. From less than \$10 million of credit claims paid in FY11 we have already paid \$23 million in FY12 and we have another \$27 million in claims pending. Even if some portion of the latter are disallowed or spill over into FY13, the level of credit claims has clearly increased sharply. Causes of the sharp increase are less clear. Taxpayer education and a possible "rush to the courthouse" due to contemplated legislative changes are possible explanations.

¹ Cities over 40,000 population: Albuquerque, Las Cruces, Rio Rancho, Santa Fe, Roswell, and Farmington. Clovis is close to 38,000 population, Hobbs is at 34,000.

2. Time period to claim credits:

Currently there is no time limit on when a credit can be claimed. This is the same treatment afforded to other credits generally, although some credits have specific time limits attached. Apparently the reasoning was that credits are not like other tax liabilities, which generally have a three year statute of limitations. As tax expenditures, credits can be viewed as more of an open-ended commitment by the state to subsidize the targeted behavior, in this case job creation. The trade-off for this relatively generous policy is that the State's potential liability for credit payments is very difficult to predict.

3. Eligible employer definition:

Current definition has two criteria either of which qualifies an employer: (1) made more than 50% of its sales to persons outside New Mexico; OR (2) is eligible for JTIP. The criteria based on sales outside the state could be interpreted to allow credit to companies that are not contributing to economic growth, for example retailers. Conversely, could be interpreted to exclude some companies that are contributing to economic growth, for example headquarters or back-office internal service providers.

4. Re-organizations:

When a company goes through a change of legal organization, it raises the question of whether the employees of the new company can be eligible for the credit because they are "new jobs" to that employer, even if substantially the same job existed prior to the re-organization. Need clarification that only genuine new jobs are eligible, not jobs that are new to the employer but not new to the state.

5. Government contracts:

This is similar to the reorganization issue. When a new company wins a government contract, can they treat the employees the "inherit" under the contract as "new jobs" for purposes of the credit? Statute should clarify that only genuine new jobs are eligible, not jobs that are new to the employer but not new to the state.

6. Wage and benefits definitions:

Current law uses Internal Revenue Code references to define wages and benefits. This definition has given rise to substantial confusion and contention. A broader definition would better meet the goals of the legislation.

7. Qualifying wage level:

The \$40,000/\$28,000 thresholds were established in 2004, which suggests they should be updated. Any changes should balance between goal of incentivizing high wages and need to target likely new businesses. An urban/rural differential makes sense, although it might be prudent to include an “extraterritorial zone” with the larger municipalities.

8. Administration

Taxpayers have raised the concern that credit claim processing has been extremely slow, reducing the incentive effects of the credit. TRD is working on streamlining the credit application process with the goal of improving timeliness of credit awards.

9. Other clean-up:

Statute should clarify that it is allowed only for jobs created “in New Mexico.”