To: Pam Ray;
Revenue Stabilization and Tax Policy Committee

From: Ethan Epstein

Date: August 28, 2012

Re: Making Certain New Mexico Income Tax Credits More Optimal Through Transferability

I. Introduction[1]

Tax expenditures can be an efficient means of targeting selected populations for benefits and also influencing the decisions of private individuals to further the goals of public policy. The roughly one hundred New Mexico's statutory tax expenditures (credits, exemptions and deductions) encompass targeted goals including economic development, poverty, health, education, renewable energy and others. While these provisions enhance some particular goal, at least with regard to New Mexico income tax credits, some, including the credits identified in this memorandum, remain *suboptimal* without transferability (i.e. the ability to trade a tax credit).

Economic theory illuminates what it means to be *optimal*. In modern vernacular, an economically efficient condition is one that promotes "win-win" possibilities. While the number of efficient choices is infinite, economists would assert that there are actions that can be taken that would make at least someone better off without making anyone else worse off. This may sound too theoretical, but, in fact, most market actions are simply trades where two parties make an exchange that makes them both better off. Inserting private market choices into the tax code is the impetus of transferability, which certainly and historically makes some people better off without making anyone worse off.

Nonetheless, most of New Mexico's tax credits are bound by rules that prevent trade, and, therefore, it is doubtful that our tax landscape is efficient enough. Accordingly, this memorandum argues that transferability, with regard to the tax credits identified below in Section IV of this memorandum, is a good choice in order to make those incentives more optimal.

[1] This memorandum is a work-in-progress and is designed to present the tax credit transferability concept for consideration during the 2012 Legislative Interim. Over the next coming months, the author will try to develop evidence of how transferability modifications are good for business and how they will help create jobs in New Mexico. Historically, transferable tax credits have been successful in creating jobs in our State. For example, the Sustainable Building Tax Credit (an transferable tax credit that promotes environmentally-friendly and efficient construction of residential and commercial structures) has inspired literally thousands of jobs in New Mexico as well as inspired other worthy achievements like making New Mexico the national leader in green residential building. Nonetheless, that type of analysis needs to be further addressed here, and I look forward to developing that perspective in the coming months for later presentation.

II. The Transferable Tax Credit System

A transferable tax credit is one that can be claimed against the holding taxpayer's tax liability and, also, sold to an unrelated taxpayer. Transferable tax credits in New Mexico have long lives and it is common for holders to sell portions of the tax credit over several years. Our State has five outright transferable credits: (1) the Affordable Housing Credit, (2) the Sustainable Building Tax Credit, (3) the Agricultural Biomass Credit, (4) the Land Conservation Incentives Tax Credit, and (5) the Rural Job Tax Credit. Over the past five years, on average, these credits have generally sold on a net between 81% and 85% on the dollar, and, accordingly appear efficient enough to promote the targeted activity from the perspective of New Mexico's Legislative Finance Committee ("LFC").[2] Also, these credits have been effective in accomplishing their respective targeted purposes.[3]

III. Transferability Comports to New Mexico's Espoused Tax Policy Principles

In the ideal, tax policy is driven by concern over a set of principles. These principles, sometimes conflicting in nature[4], provide a base against which good tax policy can be judged. The LFC has espoused the following itemized tax policy principles: (1) adequacy, (2) efficiency, (3) equity, (4) simplicity, and (5) accountability. The respective meanings of these principles are:

- Adequacy: Taxes should be just-enough to generate revenue required for provision of essential public services.

- Efficiency: Tax collection efforts should be inexpensive, or, at least not cost an inordinately-high percentage of tax revenues.

- Equity: Equal treatment of those in equal circumstances. Stated another way by the LFC, "different taxpayers should be treated fairly."

- Simplicity: Collection of taxes should be simple and understandable. If a tax system cannot be administered, then it does not matter how loftily it aspires to meet other principles.

- Accountability: Preferences should be easy to monitor and evaluate.

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[2] *See e.g., Fiscal Impact Report* associated with HB 990, 2007 Regular Legislative Session, p.4 ("Transferability is an excellent tool . . . . .[and sales of credits at 80% or more] is efficient enough to make the program worthwhile").

[3] As alluded to above in footnote 1, for example, the Sustainable Building Tax Credits effects several thousand jobs throughout our State and has also made New Mexico a national leader in green home and commercial sales. Another example is found with the conservation easement tax credit; it has allowed the State to purchase the development rights associated for roughly 10% of their value. Accordingly, the argument could reasonably be made that these programs, which are very small compared to many other incentives, are an efficient use of State money.

[4] One can see how these principles come into conflict. Progressivity requires taking more from some people than they get back directly in benefits; by distorting choices to work and save, it comes into conflict with efficiency. Simplicity sometimes competes with equal treatment of others. Therefore, it is often impossible for tax legislation to score high marks with regard to all tax policy principles.

The contemplated transferability amendments to the credits outlined in Section III follow New Mexico's principles of good tax policy noted above:

- Adequacy: Unlike suggesting a new incentive, modifying certain already-existing tax credits to be transferable, should have no effect on the government's funding. The only possible funding impact, which is near to long-term in nature, is that more people, who previously could not benefit from a particular tax incentive, begin to participate in the targeted activities because through transferability they are assured an economic return just like high income taxpayers, which the underlying incentive originally sought to encourage anyway.

- Efficiency: Transferability enhances voluntary compliance with New Mexico's tax laws because high income earners purchase credits to satisfy their tax liability before those taxes are due. Transferability, therefore, efficiently encourages timely payment of taxes.

- Equity: Only allowing rich taxpayers to economically benefit from tax credit awards exclusively by virtue of their wealth (i.e., they pay enough tax through income generation to absorb the tax credit), where poor people perform the same targeted behavior without benefit due to a low income status, avoids equal treatment for equal circumstances. Transferability corrects the inequity associated with a taxpayer's inability to use a tax credit for lack of tax liability. Equity, which mostly coincides with often-elusive and imprecisely-vague concept of fairness, is probably the strongest factor in favor of transferability.

- Simplicity: Over the past five years, New Mexico has been managing its transferable tax credit system with neither significant manpower nor weighty administrative cost. Transfers of tax credits could likely be managed by the same person who already manages transferable tax credit approvals and transfers; her management of these credits is only a small responsibility of his position.

- Accountability: Making credits transferable should not affect the State's ability to monitor and evaluate such incentives. Transferable tax credits are traced through one-page notifications to the Taxation and Revenue Department.

The most condemning attack on transferable tax policy is not from those that criticize its failure to attain any of the foregoing tax principles. Rather, some view transferability as unusual and strange - they do not understand that transferability pervades a majority of state tax systems and also exists at the Federal level. Nonetheless, within that context, transferability critics generally assert that the total benefit of the incentive does not completely inure to people who engaged in the underlying activity. This is partially true and partially not. Certainly, high income earners with sufficient tax liability who engage in the targeted behavior will seek to use the credit versus selling it at a discount because they will absorb the entire benefit without tax consequence (i.e., unlike refundable and transferable credits as described below, the use of one's credit by the one who created it is non-taxable). Therefore, this taxpayer class receives the total benefit of the credit award just like a taxpayer who receives a stationary

tax credit. Taxpayers who engage in the targeted activity who pay no or little tax economically benefit from their ability to sell the credit for cash. Taxpayer's who purchase the credit benefit by buying it at a discount, and, thus receive the benefit of tax relief. Accordingly, transferability provides for a win-win, making some people better off without disadvantaging anyone, and, thus, often represents a more optimal solution.

IV. Proposed Credits to be Modified

In reviewing all of New Mexico's tax expenditures, I have developed criteria designed to pinpoint presently-stationary tax credits that could become more optimal through transferability amendments. The five suggested credits to make transferable are identified below and the proposed first-draft statutory language is also contained at Exhibit A of this memorandum. See Exhibit A (First-Draft Statutory Language).[5] All of the below credits are income tax credits; often times New Mexico gross receipts tax credits are consumed by the credit-producing taxpayer, and, therefore, transferability would only have a marginal optimality enhancement. Tax credits that already are transferable and/or refundable are also ignored. In addition, all the below credits comport to the LFC's espoused tax policy principles relayed in Section III:

- Angel Investment Credit (NMSA § 7-2-18.17): Recently extended this year through the end of 2016, a taxpayer who files a New Mexico personal income tax return and who is an accredited investor making a qualified investment may claim a credit in an amount not to exceed 25% of not more than $100,000 of the qualified investment. In addition to reinforcing the LFC's tax policy principles, modifying these credits to become transferable will offer additional and immediate equity in the investment, which collaborates well with the underlying purpose of this incentive.

- Cultural Property Preservation Credit (NMSA §§ 7-2-18.2, 7-2A-8.6): Taxpayers may claim this credit for rehabilitating or preserving properties listed on the New Mexico Register of Cultural Properties. The credit is for one-half the cost of restoring, rehabilitating, or preserving cultural property. It may not exceed $25,000 if listed on the New Mexico Register of Cultural Properties or $50,000 if the property is within an arts and cultural district designated by the State or a municipality as designated in the Arts and Cultural District Act. This credit is similar in character to the Land Conservation Incentives Tax Credit, a transferable credit, and transferability would help non-profits and low-income people who participate in qualified preservation opportunities an economic benefit for their targeted contribution.

- Job Mentorship Program Credit (NMSA §§ 7-2-18.11, 7-2A-17.1): This credit gives an income tax credit to businesses hiring qualified students in a secondary school full-time. Credits are for 50% of the gross wages paid, subject to limitations. The amount of claims that have been made since 2006 has decreased by about one-half. Thus, offering a transferable credit for the hiring of

[5] The proposed statutory language is a rough draft in form and will likely change, albeit slightly. But, it evidences that not much statutory language needs to added in order to make the identified credits transferable.

qualified students will defray the costs of hiring such individuals, and, therefore, lead to more New Mexico students receiving jobs.

- Solar Market Development Credit (NMSA § 7-2-18.14): Taxpayers who purchase and install a solar thermal system in a residence, business, or agricultural enterprise in New Mexico, may apply for a credit up to 10% of the purchase and installation cost of the system. Like the Advanced Energy Tax Credit, allowing third-party purchases of these credits will encourage additional small-scale solar development.

- Rural Health Care Practitioners Credit (NMSA § 7-2-18.22): Eligible health care practitioners, who provide health care services in New Mexico in a rural and underserved area in a taxable year, may claim a credit, subject to certain limitations. Doctors practicing in rural areas typically earn less income than urban-practicing doctors, and, therefore, would benefit from a transferable tax credit system, which is a more equitable and optimal solution from their perspectives.

V. Transferability is Superior to Refundability

The primary alternative to transferability is refundable tax credits. Refundability means that instead of claiming your credit and/or selling it, you receive a payment from the government; refundability benefits the tax credit generator.[6] Transferability is superior to refundability for the following reasons:

- Transferability is an easier incentive to get through a state legislature that frequently balks at cash payments from the general fund to specific industries in the form of a cash rebate (e.g., the Film Tax Credit). As illogical as it may sound, it is easier for a state legislature to agree to give up money it has not collected yet (i.e., a tax credit) rather than pay out money it has already collected (i.e., a refund).

- A second benefit is that transferability allows tax credit holders to achieve a better return on the liquidation of their credit because such transactions can enjoy long-term capital gains treatment.[7] Please see the example discussed below in this Section IV on this point.

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[6] A third transferability alternative is the abnormal allowance of disproportionate allocation of tax credits through a partnership investment system (e.g., the Advanced Energy Tax Credit). Ordinarily, tax incentives are proportionally distributed in accordance with the underlying owner's interests. However, this system allows allocation of a tax credit regardless of a partner's interest in the investment (i.e., a partner could merely own 1% of the tax credit generating entity and receive the total credit benefit).

[7] Until recently, the general guidance for the tax treatment of transferable tax credits had been set forth in CCA 200211042. That technical advice from the IRS dealt with the sale of a Missouri remediation tax credit. The ruling says that on sale, the transaction becomes a disposition of property under Section 1001 of the Internal Revenue Code of 1986, as amended ("IRC"). That means that the amount realized in excess of basis would be treated as gain on the sale and recognized as income. Because the taxpayer paid nothing for the credit and it was not includable it income when it was issued, the tax basis is zero. Under that analysis, the sale will generate a gain that must be characterized as capital or ordinary. For gain to qualify as capital gain, the transaction must involve a sale or exchange as defined in IRC Section 1222 of a capital asset as defined in IRC Section 1221.

- Transferable tax credits are claimed and are generally and immediately absorbed on the taxpayer's tax return. Refunds over $10,000 require the approval of the Attorney General's office, which takes months and, thus, distracts from good and quick tax administration.

- Transferability allows credit liquidation opportunities years in advance whereas refundability occurs well after the close of the previous calendar tax year. Therefore, transferability allows credit holders to receive cash on a much quicker basis than would result from the refundable scenario.

- Transferability helps more people than cash rebates; in particular, buyers of transferable tax credits enjoy a tax break commensurate to the discount associated on the sale of the credit. The purchasers of transferable tax credits are generally New Mexico businesses that provide jobs and, in many observer's views, including mine, could use a tax break. The State also benefits from receiving a tax benefit on the sale of the credit and, as well, on the buyer's usage of the credit at a discount.[8]

- With regard to incentives that are predicated on the Federal charitable deduction, the IRS has made it clear that it will likely consider a refund a quid pro quo that would vitiate corresponding benefits under Federal tax law that require charitable intent. Transferable tax credits are not viewed as a quid pro quo. Therefore and importantly, at least in some instances, transferability better corresponds to the Federal tax system.

- Transferability provides much more flexibility than refunds by allowing people to hold their credits and stagger payments over a series of years to avoid bunching of income to mitigate a large tax burden upon liquidation.

With regard to the above second bullet point stating that transferability can provide for a better return than refundability, to support this observation, suppose we have a $100 credit held by an individual and the highest current marginal rates apply. In the refund context, the ordinary income tax rate is 40% (on both State and Federal combined basis), the total post-tax cash to the tax credit holder is:

Value of the Credit	$100

Because, in the refund context, no sale or exchange occurred income will be ordinary in nature and taxed at higher rates. However, transferable tax credits are capital and can enjoy lower capital gains rates so long as the credit has legally existed for more than one year. *See also Temple v. Comm'r*, 136 TC 15 (2011) (transferable tax credits with a holding period of more than one year receive long-term capital gain treatment on sale).

[8] Clearly, the Federal and State governments are entitled to tax on the sale of a transferable credit and on the rebate of a refundable credit. In the transferable context, tax is owed on the buyer's use of the credit as well. As previously stated, gain from the use of the credit by the buyer should be ordinary because that gain does not result from a sale or exchange as required by IRC Section 1221. CCA 200126005 holds that gain is not triggered until the credit is used on the buyer's return, and such gain is measured by the difference between the amount of the state tax saved by applying the credit and the amount paid for the credit.

Net Amount Received on a Pre-Tax Basis at 100%	$100
Combined Ordinary Rate at 39.9%[9]	($39.90)
Net Amount To Holder	$60.10

Based on the foregoing, that means, on a post-tax basis, the holder of the credit would pocket $60.10. In the transferability context, the long-term combined capital gain rate is 17.245% (on both a State and Federal combined basis). Therefore, the post-tax net amount derived is determined as follows:

Value of the Credit	$100
Net Amount Received on a Pre-Tax Basis at 82%	$82
Combined Long-Term Capital Gain Rate at 17.245%[10]	($14.14)
Net Amount To Holder	$67.86

Because $67.86 received on a post-tax basis is received in the transferable tax credit context is greater than the $60.10 in the refundable tax credit context, transferability is economically superior to refundability.[11] Stated another way, transferability generally gets more money to the credit generator than refunds do.

VI. Conclusion

The search for optimal tax policy in New Mexico has been lost in a legislative process that treats tax provisions like bits of food to be passed out as some great bargaining table in which everyone is fed something. The norms to which transferability should be referenced and tested, New Mexico's above principles of good tax policy – efficiency, equal treatment of equals, simplicity, revenues sufficient to meet expenditure requirements – are enhanced without harm to the others with transferable tax credits. Amending the tax credits identified in Section IV to include transferability promotes a win-win result. Because the tax credit generators, the tax credit buying community, and the State all benefit from transferable tax credits, amending the incentives identified in this memorandum would promote a more optimal tax system.

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[9] The highest marginal individual Federal rate of 35% coupled with the New Mexico rate of 4.9%.

[10] The Federal long-term capital gain rate of 15% coupled with New Mexico's rate of 4.9% with New Mexico exclusion adjustments provide in NMSA § 7-2-34(A)(2)(e) (i.e., New Mexico tax law allows for a 50% income reduction in the gain recognized from the sale of a capital asset like a transferable tax credit).

[11] In instances where the credit is sold for a greater price (e.g., 85%) the economic superiority of transferability is commensurately enhanced. Also, even as income decreases and, likewise the associated tax brackets decrease, transferability remains superior to refundability because of the capital gain rate advantage over ordinary rate taxation. Examples of this relationship can be provided upon request.

SENATE BILL

51ST LEGISLATURE - STATE OF NEW MEXICO - FIRST SESSION, 2013

INTRODUCED BY

DISCUSSION DRAFT

AN ACT

RELATING TO TAXATION; AUTHORIZING CERTAIN TAX CREDITS TO BE TRANSFERRED BETWEEN TAXPAYERS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF NEW MEXICO:

SECTION 1. Section 7-2-18.11 NMSA 1978 (being Laws 2003, Chapter 400, Section 1) is amended to read:

"7-2-18.11. JOB MENTORSHIP TAX CREDIT.--

A. To encourage New Mexico businesses to hire youth participating in career preparation education programs, a taxpayer who files an individual New Mexico income tax return, who is not a dependent of another individual and who is an owner of a New Mexico business may claim a credit in an amount equal to fifty percent of gross wages paid to qualified students who are employed by the business during the taxable year for which the return is filed. The tax credit provided by

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this section may be referred to as the "job mentorship tax credit".

B. A taxpayer who is an owner of a New Mexico business may claim the job mentorship tax credit for each taxable year in which the business employs one or more qualified students. The maximum aggregate credit allowable shall not exceed fifty percent of the gross wages paid to not more than ten qualified students employed by the business for up to three hundred twenty hours of employment of each qualified student in each taxable year for a maximum of three taxable years for each qualified student. In no event shall a taxpayer claim a credit in excess of twelve thousand dollars ($12,000) in any taxable year. The taxpayer shall certify that hiring the qualified student does not displace or replace a current employee.

C. The department shall issue job mentorship tax credit certificates upon request to any accredited New Mexico secondary school that has a school-sanctioned career preparation education program. The maximum number of certificates that may be issued in a school year to any one school is equal to the number of qualified students in the school-sanctioned career preparation education program on October 15 of that school year, as certified by the school principal.

D. A job mentorship tax credit certificate may be

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executed by a school principal with respect to a qualified student, and the executed certificate may be transferred to a New Mexico business that employs that student. By executing the certificate with respect to a student, the school principal certifies that the school has a school-sanctioned career preparation education program and the student is a qualified student.

E. To claim the job mentorship tax credit, the taxpayer must submit with respect to each employee for whom the credit is claimed:

(1) a properly executed job mentorship tax credit certificate;

(2) information required by the secretary with respect to the employee's employment by the business during the taxable year for which the credit is claimed; and

(3) information required by the secretary that the employee was not also employed in the same taxable year by another New Mexico business qualifying for and claiming a job mentorship tax credit for that employee pursuant to this section or the Corporate Income and Franchise Tax Act. If the requirements of this section have been complied with, the department shall approve the claim for the credit and issue a document pursuant to Subsection G of this section.

F. The job mentorship tax credit may only be deducted from [~~the~~] a taxpayer's New Mexico income tax

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liability for the taxable year. Any portion of the maximum credit provided by this section that remains unused at the end of the taxpayer's taxable year may be carried forward for three consecutive taxable years; provided the total credits claimed under this section shall not exceed the maximum allowable pursuant to Subsection B of this section.

G. If the requirements of this section have been complied with, the department shall issue to the applicant a document granting the tax credit allowed pursuant to this section. The document shall be numbered for identification and shall declare its date of issuance and the amount of the tax credit allowed pursuant to this section. The document may be submitted by the applicant with that taxpayer's income tax return or may be sold, exchanged or otherwise transferred to another taxpayer. The parties to such a transaction shall notify the department of the sale, exchange or transfer within ten days of the sale, exchange or transfer. Credits shall only be transferred in increments of ten thousand dollars ($10,000) or more. A tax credit or increment of a tax credit may only be transferred once.

[~~G.~~] H. A husband and wife who file separate returns for a taxable year in which they could have filed a joint return may each claim only one-half of the credit that would have been allowed on a joint return.

[~~H.~~] I. A taxpayer who otherwise qualifies for and

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claims a job mentorship tax credit for employment of qualified students by a partnership, limited partnership, limited liability company, S corporation or other business association of which the taxpayer is a member may claim a credit only in proportion to [~~his~~] the taxpayer's interest in the partnership, limited partnership, limited liability company, S corporation or association. The total credit claimed by all members of the business shall not exceed the maximum credit allowable pursuant to Subsection B of this section.

[~~I.~~] J. As used in this section:

(1) "career preparation education program" means a work-based learning or school-to-career program designed for secondary school students to create academic and career goals and objectives and find employment in a job meeting those goals and objectives;

(2) "New Mexico business" means a partnership, limited partnership, limited liability company treated as a partnership for federal income tax purposes, S corporation or sole proprietorship that carries on a trade or business in New Mexico and that employs in New Mexico fewer than three hundred full-time employees at any one time during the taxable year; and

(3) "qualified student" means an individual who is at least fourteen years of age but not more than twenty-one years of age who is attending full time an accredited New

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Mexico secondary school and who is a participant in a career preparation education program sanctioned by the secondary school."

SECTION 2. Section 7-2-18.14 NMSA 1978 (being Laws 2006, Chapter 93, Section 1, as amended) is amended to read:

"7-2-18.14. SOLAR MARKET DEVELOPMENT TAX CREDIT--RESIDENTIAL AND SMALL BUSINESS SOLAR THERMAL AND PHOTOVOLTAIC MARKET DEVELOPMENT TAX CREDIT.--

A. Except as provided in Subsection C of this section, a taxpayer who files an individual New Mexico income tax return for a taxable year beginning on or after January 1, 2006 and who purchases and installs after January 1, 2006 but before December 31, 2016 a solar thermal system or a photovoltaic system in a residence, business or agricultural enterprise in New Mexico owned by that taxpayer may apply for, and the department may allow, a solar market development tax credit of up to ten percent of the purchase and installation costs of the system.

B. The total solar market development tax credit allowed for either a photovoltaic system or a solar thermal system shall not exceed nine thousand dollars ($9,000). The department shall allow solar market development tax credits only for solar thermal systems and photovoltaic systems certified by the energy, minerals and natural resources department.

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C. Solar market development tax credits may not be claimed or allowed for:

(1) a heating system for a swimming pool or a hot tub; or

(2) a commercial or industrial photovoltaic system other than an agricultural photovoltaic system on a farm or ranch that is not connected to an electric utility transmission or distribution system.

D. The department may allow a maximum annual aggregate of:

(1) two million dollars ($2,000,000) in solar market development tax credits for solar thermal systems; and

(2) three million dollars ($3,000,000) in solar market development tax credits for photovoltaic systems.

E. The solar market development tax credit may only be deducted from a taxpayer's income tax liability. A portion of the solar market development tax credit that remains unused in a taxable year may be carried forward for a maximum of ten consecutive taxable years following the taxable year in which the credit originates until fully expended.

F. If the requirements of this section have been complied with, the department shall issue to the applicant a document granting the tax credit allowed pursuant to this section. The document shall be numbered for identification

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and shall declare its date of issuance and the amount of the tax credit allowed pursuant to this section. The document may be submitted by the applicant with that taxpayer's income tax return or may be sold, exchanged or otherwise transferred to another taxpayer. The parties to such a transaction shall notify the department of the sale, exchange or transfer within ten days of the sale, exchange or transfer. Credits shall only be transferred in increments of ten thousand dollars ($10,000) or more. A tax credit or increment of a tax credit may only be transferred once.

[~~F.~~] G. Prior to July 1, 2006, the energy, minerals and natural resources department shall adopt rules establishing procedures to provide certification of solar thermal systems and photovoltaic systems for purposes of obtaining a solar market development tax credit. The rules shall address technical specifications and requirements relating to safety, code and standards compliance, solar collector orientation and sun exposure, minimum system sizes, system applications and lists of eligible components. The energy, minerals and natural resources department may modify the specifications and requirements as necessary to maintain a high level of system quality and performance.

[~~G.~~] H. As used in this section:

(1) "photovoltaic system" means an energy system that collects or absorbs sunlight for conversion into

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electricity; and

(2) "solar thermal system" means an energy system that collects or absorbs solar energy for conversion into heat for the purposes of space heating, space cooling or water heating."

SECTION 3. Section 7-2-18.17 NMSA 1978 (being Laws 2007, Chapter 172, Section 1, as amended) is amended to read:

"7-2-18.17. ANGEL INVESTMENT CREDIT.--

A. A taxpayer who files a New Mexico income tax return, is not a dependent of another taxpayer, is an accredited investor and makes a qualified investment may claim a credit in an amount not to exceed twenty-five percent of not more than one hundred thousand dollars ($100,000) of the qualified investment. The tax credit provided in this section shall be known as the "angel investment credit".

B. A taxpayer may claim the angel investment credit for not more than two qualified investments in a taxable year; provided that each investment is in a different qualified business. A taxpayer may claim the angel investment credit for qualified investments made in the same qualified business or successor of that business for not more than three taxable years. The angel investment credit shall not exceed twenty-five thousand dollars ($25,000) for each qualified investment by the taxpayer.

C. A taxpayer may claim the angel investment

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credit no later than one year following the end of the calendar year in which the qualified investment was made; provided that a claim for the credit may not be made or allowed with respect to any investment made after December 31, 2016.

D. A taxpayer shall apply for certification of eligibility for the angel investment credit from the economic development department. Applications shall be considered in the order received. If the economic development department determines that the taxpayer is an accredited investor and the investment is a qualified investment, [~~it~~] the department shall issue a certificate of eligibility to the taxpayer, subject to the limitation in Subsection E of this section. The certificate shall be dated and shall include a calculation of the amount of the angel investment credit for which the taxpayer is eligible. The economic development department may issue rules governing the procedure for administering the provisions of this subsection.

E. The economic development department may issue a certificate of eligibility pursuant to Subsection D of this section only if the total amount of angel investment credits represented by certificates of eligibility issued by the economic development department in any calendar year will not exceed seven hundred fifty thousand dollars ($750,000). If the applications for certificates of eligibility for angel

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investment credits represent an aggregate amount exceeding seven hundred fifty thousand dollars ($750,000) for any calendar year, certificates shall be issued in the order that the applications were received. The excess applications that would have been certified, but for the limit imposed by this subsection, shall be certified, subject to the same limit, in subsequent calendar years.

F. The economic development department shall report annually to the legislative finance committee on the utilization and effectiveness of the angel investment credit. The report shall include, at a minimum: the number of accredited investors to whom certificates of eligibility were issued by the department in the previous year; the names of those investors; the amount of angel investment credit for which each investor was certified eligible; and the number and names of the businesses that the department has determined are qualified businesses for purposes of an investment by an accredited investor. The report shall also include an evaluation of the success of the angel investment credit as an incubator of new businesses in New Mexico and of the continued viability and operation in New Mexico of businesses in which investments eligible for the angel investment credit have been made.

G. To claim the angel investment credit, the taxpayer must provide to the taxation and revenue department a

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certificate of eligibility issued by the economic development department pursuant to Subsection D of this section and any other information the taxation and revenue department may require to determine the amount of the tax credit due the taxpayer. If the requirements of this section have been complied with, the taxation and revenue department shall approve the claim for the credit and issue a document pursuant to Subsection K of this section.

H. A taxpayer who otherwise qualifies for and claims a credit pursuant to this section for a qualified investment made by a partnership or other business association of which the taxpayer is a member may claim a credit only in proportion to the taxpayer's interest in the partnership or business association. The total credit claimed in the aggregate by all members of the partnership or business association in a taxable year with respect to a qualified investment shall not exceed twenty-five thousand dollars ($25,000).

I. A husband and wife who file separate returns for a taxable year in which they could have filed a joint return may each claim one-half of the credit that would have been allowed on a joint return.

J. The angel investment credit may only be deducted from [~~the~~] a taxpayer's income tax liability. Any portion of the tax credit provided by this section that

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remains unused at the end of the taxpayer's taxable year may be carried forward for three consecutive years.

K. If the requirements of this section have been complied with, the department shall issue to the applicant a document granting the tax credit allowed pursuant to this section. The document shall be numbered for identification and shall declare its date of issuance and the amount of the tax credit allowed pursuant to this section. The document may be submitted by the applicant with that taxpayer's income tax return or may be sold, exchanged or otherwise transferred to another taxpayer. The parties to such a transaction shall notify the department of the sale, exchange or transfer within ten days of the sale, exchange or transfer. Credits shall only be transferred in increments of ten thousand dollars ($10,000) or more. A tax credit or increment of a tax credit may only be transferred once.

[~~K.~~] L. As used in this section:

(1) "accredited investor" means a person who is an accredited investor within the meaning of Rule 501 issued by the federal securities and exchange commission pursuant to the federal Securities Act of 1933, as amended;

(2) "business" means a corporation, general partnership, limited partnership, limited liability company or other similar entity, but excludes an entity that is a government or a nonprofit organization designated as such by

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the federal government or any state;

(3) "equity" means common or preferred stock of a corporation, a partnership interest in a limited partnership or a membership interest in a limited liability company, including debt subject to an option in favor of the creditor to convert the debt into common or preferred stock, a partnership interest or a membership interest;

(4) "high-technology research" means research:

(a) that is undertaken for the purpose of discovering information that is technological in nature and the application of which is intended to be useful in the development of a new or improved business component of the qualified business; and

(b) substantially all of the activities of which constitute elements of a process or experimentation related to a new or improved function, performance, reliability or quality, but not related to style, taste or cosmetic or seasonal design factors;

(5) "manufacturing" means combining or processing components or materials to increase their value for sale in the ordinary course of business, but does not include:

(a) construction;

(b) farming;

(c) processing natural resources,

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including hydrocarbons; or

(d) preparing meals for immediate consumption, on- or off-premises;

(6) "qualified business" means a business that:

(a) maintains its principal place of business in New Mexico;

(b) engages in high-technology research or manufacturing activities in New Mexico;

(c) is not primarily engaged in or is not primarily organized as any of the following types of businesses: credit or finance services, including banks, savings and loan associations, credit unions, small loan companies or title loan companies; financial brokering or investment; professional services, including accounting, legal services, engineering and any other service the practice of which requires a license; insurance; real estate; construction or construction contracting; consulting or brokering; mining; wholesale or retail trade; providing utility service, including water, sewerage, electricity, natural gas, propane or butane; publishing, including publishing newspapers or other periodicals; broadcasting; or providing internet operating services;

(d) has not issued securities registered pursuant to Section 6 of the federal Securities Act

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of 1933, as amended; has not issued securities traded on a national securities exchange; is not subject to reporting requirements of the federal Securities Exchange Act of 1934, as amended; and is not registered pursuant to the federal Investment Company Act of 1940, as amended, at the time of the investment;

(e) has one hundred or fewer employees calculated on a full-time-equivalent basis at the time of the investment; and

(f) has not had gross revenues in excess of five million dollars ($5,000,000) in any fiscal year ending on or before the date of the investment; and

(7) "qualified investment" means a cash investment in a qualified business for equity, but does not include an investment by a taxpayer if the taxpayer, a member of the taxpayer's immediate family or an entity affiliated with the taxpayer receives compensation from the qualified business in exchange for services provided to the qualified business within one year of investment in the qualified business."

SECTION 4. Section 7-2A-17.1 NMSA 1978 (being Laws 2003, Chapter 400, Section 2) is amended to read:

"7-2A-17.1. JOB MENTORSHIP TAX CREDIT.--

A. To encourage New Mexico businesses to hire youth participating in career preparation education programs,

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a taxpayer that is a New Mexico business and that files a corporate income tax return may claim a credit in an amount equal to fifty percent of gross wages paid to qualified students who are employed by the taxpayer during the taxable year for which the return is filed. The tax credit provided by this section may be referred to as the "job mentorship tax credit".

B. A taxpayer may claim the job mentorship tax credit provided in this section for each taxable year in which the taxpayer employs one or more qualified students. The maximum aggregate credit allowable shall not exceed fifty percent of the gross wages paid to not more than ten qualified students employed by the taxpayer for up to three hundred twenty hours of employment of each qualified student in each taxable year for a maximum of three taxable years for each qualified student. In no event shall a taxpayer claim a credit in excess of twelve thousand dollars ($12,000) in any taxable year. The employer shall certify that hiring the qualified student does not displace or replace a current employee.

C. The department shall issue job mentorship tax credit certificates upon request to any accredited New Mexico secondary school that has a school-sanctioned career preparation education program. The maximum number of certificates that may be issued in a school year to any one

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school is equal to the number of qualified students in the school-sanctioned career preparation education program on October 15 of that school year, as certified by the school principal.

D. A job mentorship tax credit certificate may be executed by a school principal with respect to a qualified student, and the executed certificate may be transferred to a New Mexico business that employs that student. By executing the certificate with respect to a student, the school principal certifies that the school has a school-sanctioned career preparation education program and the student is a qualified student.

E. To claim the job mentorship tax credit, the taxpayer must submit with respect to each employee for whom the credit is claimed:

(1) a properly executed job mentorship tax credit certificate;

(2) information required by the secretary with respect to the employee's employment by the taxpayer during the taxable year for which the credit is claimed; and

(3) information required by the secretary that the employee was not also employed in the same taxable year by another New Mexico business qualifying for and claiming a job mentorship tax credit for that employee pursuant to this section or the Income Tax Act. If the

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requirements of this section have been complied with, the department shall approve the claim for the credit and issue a document pursuant to Subsection G of this section.

F. The job mentorship tax credit may only be deducted from [~~the~~] a taxpayer's corporate income tax liability for the taxable year. Any portion of the maximum credit provided by this section that remains unused at the end of the taxpayer's taxable year may be carried forward for three consecutive taxable years; provided the total credits claimed pursuant to this section shall not exceed the maximum allowable under Subsection B of this section.

G. If the requirements of this section have been complied with, the department shall issue to the applicant a document granting the tax credit allowed pursuant to this section. The document shall be numbered for identification and shall declare its date of issuance and the amount of the tax credit allowed pursuant to this section. The document may be submitted by the applicant with that taxpayer's corporate income tax return or may be sold, exchanged or otherwise transferred to another taxpayer. The parties to such a transaction shall notify the department of the sale, exchange or transfer within ten days of the sale, exchange or transfer. Credits shall only be transferred in increments of ten thousand dollars ($10,000) or more. A tax credit or increment of a tax credit may only be transferred once.

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[~~G.~~] H. As used in this section:

(1) "career preparation education program" means a work-based learning or school-to-career program designed for secondary school students to create academic and career goals and objectives and find employment in a job meeting those goals and objectives;

(2) "New Mexico business" means a corporation that carries on a trade or business in New Mexico and that employs in New Mexico fewer than three hundred full-time employees during the taxable year; and

(3) "qualified student" means an individual who is at least fourteen years of age but not more than twenty-one years of age who is attending full time an accredited New Mexico secondary school and who is a participant in a career preparation education program sanctioned by the secondary school."

SECTION 5. APPLICABILITY.--The provisions of this act apply to taxable years beginning on or after January 1, 2014.

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