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FISCAL IMPACT REPORT

ORIGINAL DATE 02/02/16

SPONSOR Campos LAST UPDATED _____ HB _____

SHORT TITLE Small Business Investment Tax Credit SB 133

ANALYST Alejandro

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY16	FY17	FY18	FY19	FY20		
(\$0)	(\$450.0- 2,000.0)	(\$850.0- 2,000.0)	(\$1,250.0- 2,000.0)	(\$1,650.0- 2,000.0)	Recurring	General Fund

Parenthesis () indicate revenue decreases

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

FY16	FY17	FY18	3-Year Total	Recurring or Nonrecurring	Fund Affected
\$48.7	\$16.7	\$16.7	\$82.1	Recurring	TRD Budget

Parenthesis () indicate expenditure decreases

SOURCES OF INFORMATION

LFC Files

Responses Received From

Economic Development Department (EDD)

Taxation and Revenue Department (TRD)

SUMMARY

Senate Bill 133 enacts a new section of the Income Tax Act to create the “small business investment income tax credit.” The bill would allow a taxpayer who is an accredited investor, as defined by SEC Rule 501, to submit a claim for a credit up to 25 percent of not more than \$250 thousand of a qualified investment.

The bill limits the claim of the tax credit by a taxpayer to a maximum of five qualified investments in a taxable year, provided that each investment is in a different qualified business. In the case of qualified investments made in the same qualified business or successor of that business, the bill establishes a maximum of three taxable years. Also, the portion of the tax credit

that exceeds a taxpayer's tax liability in the taxable year in which the credit is claimed may be carried forward for a maximum of five consecutive taxable years.

SB 133 includes reporting requirements. The bill requires taxpayers applying for the credit to provide information to the Economic Development Department (EDD) concerning the taxpayer's investment accreditation requirements. The bill further requires EDD to promulgate rules establishing procedures to certify qualified accredited investors for purposes of obtaining the credit. EDD must issue a dated and sequentially-numbered certificate of eligibility containing a list of the qualified small business investors claiming the credit that includes personal identifiable information.

The bill also requires EDD to report annually on the number of accredited investors to whom certificates of eligibility were issued by the department in the previous year and the number and names of the businesses that the department has determined are qualified for the purpose of the investment. The bill requires the appropriate legislative committees to review the effectiveness and cost of the tax credit to evaluate the success of the credit as an incubator of new businesses in New Mexico.

There is no effective date of this bill. It is assumed that the new effective date is 90 days after this session ends (May 18, 2016). The provisions of the act apply to taxable years beginning on or after January 1, 2016.

FISCAL IMPLICATIONS

Due to the broad definition for qualified business in this bill, LFC staff believes this credit will have a substantial taxpayer application and most likely reach the \$2 million cap on a recurring basis. TRD predicts that the credit will phase-in over time, reaching the cap closer to FY20.

According to TRD analysis, the bill implicates principles of efficiency and simplicity. SB 133 is very similar to the angel investment credit. However, there are several differences: (1) the angel investment credit is limited to research and manufacturing businesses, whereas the bill would apply to other business types that are not excluded, such as agriculture, forestry, fishing, hunting, transportation and warehousing, waste management, education services, healthcare and social assistance, arts, entertainment and recreation, accommodation and food service, and personal service businesses; and (2) the angel investment credit limits investments by investment round, whereas this credit allows for investments in the same company for three years. Otherwise, the two credits are very similar. While the angel investment credit was being utilized, as originally enacted, it was perceived as too limited, and was therefore amended during the 2015 session to broaden credit availability. From an efficiency perspective, it may be prudent to collect data and study the effectiveness of the angel investment credit before enacting a broader duplicate at the same credit amounts and thresholds.

From a simplicity perspective, TRD also indicates that it would seem that the goals of this bill could be accomplished through amendments to the angel investment credit, rather than enacting an entirely new credit. Consideration should be given to amending to reduce administrative and compliance burdens for taxpayer and the administering agencies (TRD and EDD).

While this bill considers exclusivity – it prohibits the angel investment credit and other credits from being taken with respect to the same investment, adding another credit effectively expands the total investments for which a taxpayer can claim a credit to ten.

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.

TECHNICAL ISSUES

TRD indicates that the language of the bill regarding applying for multiple credits is unclear (page 2, Subsection E). Administering the proposed limitation may be onerous. Rules, regulations, policies, and procedures will be necessary to manage eligibility, carry-forwards, and other aspects of the program.

There is tension in the statutory language that should be corrected. Subsection D (p. 2; ll. 13-16) prescribes that the claim must be made within one year of making the investment. Yet, Subsection G (p. 3; ll. 22-25) contemplates and allows a queue that may render the one-year claim limitation impracticable.

This bill does not contain a delayed repeal date. The LFC recommends adding a delayed repeal date.

ADMINISTRATIVE IMPLICATIONS

This bill would require EDD to determine whether investors and businesses are qualified for the credit and to issue certificates of eligibility to the taxpayer. The EDD may issue rules governing the procedure for administering the credit and ensure that certificates do not exceed the cap of \$2 million in any calendar year. EDD believes that this bill would necessitate the addition of one FTE depending on the workload associated with qualifying companies and individual investors, as well as tracking and reporting.

TRD indicates that the bill does not impact the financial distribution process, but the credit may be subject to the financial disclosure requirements per Governmental Accounting Standards Board (GASB) Statement No.77. GASB 77 disclosure statements are effective for financial statements for periods beginning after December 15, 2015. An assessment of the credit against the tax abatement criteria specified in GASB 77 will need to be performed by TRD. If the credit meets the criteria, then the disclosure is required in TRD's financial statements.