# SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 1494

SPONSOR: Commerce, Economic Opportunities, and Consumer Services Committee and Senator Garcia

SUBJECT: Qualified Target Industry and Qualified Defense Contractor Tax Refund Programs

DATE: April 13, 2004 REVISED:

| | ANALYST | STAFF DIRECTOR | REFERENCE | ACTION |
|---|---|---|---|---|
| 1. | Cibula | Maclure | CM | Favorable/CS |
| 2. | Dodson | Skelton | HP | Favorable |
| 3. | | | FT | Withdrawn |
| 4. | Kelly | Kelly | ATD | Favorable |
| 5. | | | AP | Withdrawn: Favorable |
| 6. | | | | |

## I. Summary:


The committee substitute implements the recommendations from Interim Project Report 2004-115, *Review of Qualified Target Industry and Qualified Defense Contractor Tax Refund Programs*.[1] In accordance with the recommendations in the report, the committee substitute:

- Extends the authority for the programs for an additional five years.
- Clarifies that tax refund agreements in existence when the statutory authority for the programs expires continue in effect.
- Clarifies that the qualified defense contractor tax refund program may be used to retain jobs.
- Requires claims for tax refunds to be paid in the order approved.
- Directs the Office of Tourism, Trade, and Economic Development to attempt to amend existing tax refund agreements created under the qualified target industry tax refund program to require tax refund claims to be submitted by January 31 for the net new full time equivalent Florida jobs as of December 31, and requires Enterprise Florida, Inc., to discuss progress toward amending the agreements in its annual report on economic development programs.

The committee substitute substantially amends the following sections of the Florida Statutes: 288.095, 288.1045, and 288.106.


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[1] Committee on Commerce, Economic Opportunities, and Consumer Services, The Florida Senate, Interim Project Report 2004-115, *Review of Qualified Target Industry and Qualified Defense Contractor Tax Refund Programs*, December 2003, *available at* http://www.flsenate.gov/data/Publications/2004/Senate/reports/interim_reports/pdf/2004-115cm.pdf.

## II. Present Situation:

The qualified target industry (QTI) and qualified defense contractor (QDC) tax refund programs are tools used by the state to encourage businesses to locate or expand in this state and provide high-wage jobs for Floridians. Businesses participating in the programs may receive tax refunds based on the number of qualifying jobs and the average wage of their employees. The QTI and QDC programs are scheduled to expire or close to new activity on June 30, 2004.

An interim project report by the Senate Committee on Commerce, Economic Opportunities, and Consumer Services, titled *Review of Qualified Target Industry and Qualified Defense Contractor Tax Refund Programs*, recommended that the programs be continued by the Legislature as a relatively low-cost method to compete with other states for jobs. According to the report, Florida faces competition from many states offering economic development incentives for job creation. The report also found that the programs do not perfectly discriminate between businesses that would locate or expand operations in Florida without incentives and those for which an incentive is needed to induce the business to locate or expand operations in Florida. However, the availability of incentives was a deciding factor for the creation of some jobs. Lastly, the report found that the qualified target industry tax refund program has been substantially over-funded over the past few years, to the detriment of other legislative priorities. To minimize over-funding the QTI program, the report recommended that claims for tax refunds be submitted by January 31 for jobs created as of December 31 of the preceding calendar year. If tax refund claims are received by OTTED by January 31, the tax refund claims will be able to be taken into account during the next budgeting process.[2]

Other recommendations in the report included the following:

- The authority for the programs should expire June 30, 2009, to encourage a future Legislature to review the performance of the programs.
- Tax refund agreements in effect when the authority for the programs expires should continue in effect in accordance with their terms.
- The statutory authority for the qualified defense contractor tax refund program should clarify the program may be used to retain jobs.[3]

### QTI Program

A qualified target industry (QTI) business may receive a tax refund equal to the tax refund per job times the number of jobs created, pursuant to a tax refund agreement with the Office of Tourism, Trade, and Economic Development (OTTED).[4] The tax refund per job is between $3,000 and $8,000, depending upon the average salary of the jobs created and whether the jobs are located within a rural county or enterprise zone (EZ).[5] See Table 1. Taxes that may be refunded under the program include corporate income taxes; insurance premium taxes; taxes on

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[2] *Id.*
[3] *Id.*
[4] Section 288.106(2), F.S.
[5] Section 288.106(2)(b), F.S.

sales, use, and other transactions; intangible personal property taxes; emergency excise taxes; excise taxes on documents; and certain ad valorem taxes.

Table 1. Tax Refund Available Per Job

| TAX REFUND PER JOB | LOCATION OF NEW JOBS | PERCENT OF AVERAGE WAGE |
|---|---|---|
| $3,000 | Statewide | 115% |
| $4,000 | Statewide | 150% |
| $5,000 | Statewide | 200% |
| $6,000 | Rural County or EZ | 115% |
| $7,000 | Rural County or EZ | 150% |
| $8,000 | Rural County or EZ | 200% |

The total tax refund must be paid to a business over a 4-year or longer period.[6] The maximum refund that a business may receive in any year is $1.5 million or, if the business is located in an enterprise zone, $2.5 million.[7] The total refund that a business may receive may not exceed $5 million or, if the business is located in an enterprise zone, $7.5 million.[8] The total amount of tax refunds that OTTED may schedule for payment under the QTI and QDC programs may not exceed $35 million in any fiscal year.[9]

To be eligible for tax refunds under the QTI program, a target industry business must apply to OTTED for certification as a qualified target industry business before it decides to locate a new business in this state or to expand an existing business in this state.[10] Then the business must enter into a performance-based contract with OTTED to create a specific number of high-wage jobs.

A target industry business is a corporate headquarters or a business within a list of target industries developed by OTTED in consultation with Enterprise Florida, Inc., (EFI).[11] OTTED must submit this list to the Legislature with its final agency legislative budget request.[12] Industries selected for the list must meet the following criteria: expected to have future growth in employment and output, provide stable employment not subject to layoffs, provide high wages, be independent of Florida markets and resources, diversify the state's economic base, and benefit the state and regional economies.[13] The industries contained on the target industries list include certain manufacturing facilities; finance and insurance services; wholesale trade; information services; professional, scientific, and technical services; management services; and administrative support.[14] Additionally, defense industry businesses may be target industry businesses.

[6] *See* s. 288.106(2)(b), F.S.
[7] *Id.*
[8] *Id.*
[9] 288.095(3)(a), F.S.
[10] Section 288.106(3)(a), F.S. It appears that the purpose of this limitation is to prevent the payment of tax refunds to businesses that had planned to locate a new business or expand an existing business in Florida anyway.
[11] Section 288.106(1)(o), F.S.
[12] *Id.*
[13] *Id.*
[14] For the complete list of target industries, see OTTED's *Legislative Budget Request 2004-2005,* at 93.

In its application for certification, a target industry business must describe its proposed new business or expansion of an existing business.[15] The description of proposed operations must provide for the creation of jobs that have an average salary of at least 115 percent of the average private sector wage in the area where the business is to be located or the statewide average private sector wage.[16] OTTED, however, may waive the average wage requirement of the QTI program in limited circumstances.[17] A new or expanding business must propose the creation of at least 10 jobs.[18] An expanding business must also propose to increase its real and personal property resulting in a 10-percent net increase in employment in this state.[19]

The application must also be accompanied by a resolution from the county or municipality in which the business will be located.[20] The resolution must recommend that the business be certified as a qualified target industry business and commit the county or municipality to provide local financial support.[21] The local financial support must equal at least 20 percent of the tax refund available under the program for the business to be eligible for a full refund.[22] This financial support is typically called the 20-percent local match. The business may have to agree to the local government's terms and conditions for eligibility for the local match.

If the business proposes to locate in a brownfield area or in a rural county or certain counties contiguous to a rural county, local financial support is optional.[23] If a local government chooses to exercise the option to be exempt from the local financial support requirements of the program, then the business is not eligible for more than 80 percent of the tax refunds that would otherwise be available to it under the program.[24]

Upon receipt of a completed application, OTTED must review the application based on, but not limited to, the following criteria:

1. Expected contributions to the state strategic economic development plan adopted by Enterprise Florida, Inc.,
2. The economic benefit of the jobs created by the project in this state.
3. The amount of capital investment to be made by the applicant in this state.
4. The local commitment and support for the project.
5. The effect of the project on the local community.

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[15] Section 288.106(3), F.S.
[16] Section 288.106(3)(a)4. and (3)(b)1., F.S. OTTED requires that the average salary of jobs created be 115 percent of the lower of the average private sector wage in the area or the statewide private sector wage.
[17] Section 288.106(3)(b)1., F.S. According to OTTED, it has waived the minimum average wage requirements of the QTI program fewer than five times.
[18] Section 288.106(3)(b)2., F.S.
[19] Section 288.106(1)(g) and (3)(b)2., F.S.
[20] Section 288.106(3)(a)9., F.S.
[21] *Id.*
[22] Section 288.106(3)(f), F.S.
[23] Section 288.106(1)(k), F.S.
[24] *Id.*

6. The effect of any tax refunds [under the QTI program] on the viability of the proposed operations and the probability that the proposed operations will be undertaken in this state.
7. The expected long-term commitment to this state.
8. A review of the business's past activities in this state or other states.[25]

Although OTTED must consider these criteria, the criteria do not establish minimum standards that must be met for certification, nor do the criteria require OTTED to certify any business as a QTI business. If the application is approved, the OTTED director, by letter, will certify the business as a QTI business and state the value of the tax refund available to the business.[26]

After a business is certified as a QTI business, it may enter into a tax refund agreement with OTTED.[27] The agreement typically will incorporate the application for certification as a QTI business, and the proposed number of jobs and salary projections will become contract requirements. The contract also will clearly state that the agreement to pay tax refunds is contingent upon appropriations from the Legislature.[28]

A business that was certified as a QTI business after May 30, 2002, must file its claim for a tax refund by January 31 each year.[29] A business that was certified as a QTI business before May 30, 2002, may file a claim for a tax refund any time prior to June 15.[30] If a business does not timely submit a claim for refunds, it will be terminated from the QTI program.[31]

Sharpton, Brunson and Company (SBC), an outside contractor hired by OTTED, processes the claims for tax refunds under the QTI program.[32] To process refund claims, SBC verifies job creation and average wages through unemployment compensation insurance information, company data, and on-site audits. SBC verifies the amount of taxes paid by a QTI business by examining receipts, tax bills, and copies of checks submitted in payment of tax bills.

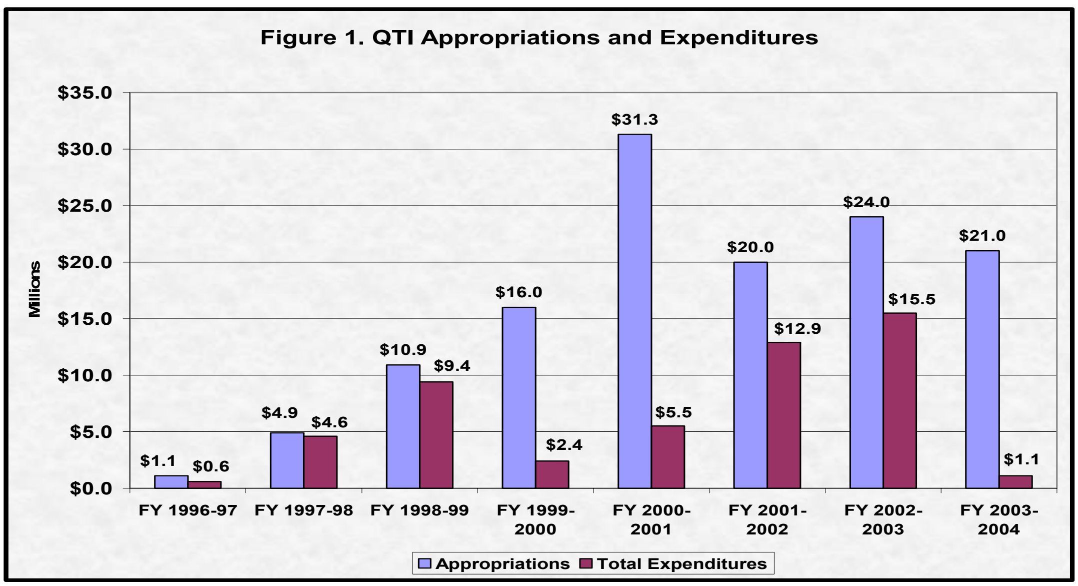
If a QTI business satisfies the job-creation and wage requirements in its contract with OTTED, pays sufficient taxes, and OTTED receives the necessary local financial support, the business will receive the full tax refund specified in its agreement. If a QTI business fails to fully comply with its job-creation and salary requirements, it may receive a prorated tax refund less a 5-percent penalty.[33] To be eligible for a prorated refund, the business must achieve at least 80 percent of its projected employment, and the average wage paid by the business must be at least

[25] Section 288.106(3)(c), F.S.
[26] Section 288.106(3)(e)1. and (f), F.S.
[27] Section 288.106(3)(e)2., F.S.
[28] Section 288.106(4)(d), F.S.
[29] Section 288.106(5)(a), F.S.
[30] Auditor General, *Tax Refund Program for Qualified Target Industry Businesses Administered by the Executive Office of the Governor: Operational Audit*, Report No. 01-080, January 2001, at 3.
[31] Section 288.106(4)(b), F.S.
[32] Sharpton, Brunson and Company fulfills certain administrative-support functions for the following programs: Economic Development Transportation Fund, Qualified Target Industry Tax Refund Program, Community Contribution Tax Credit Program, Urban Jobs Tax Credit, and the Rural Jobs Tax Credit. The term of SBC's contract with OTTED is from April 1, 2002, through June 30, 2004, at a rate of $500,000 per year.
[33] Section 288.106(5)(d), F.S.

90 percent of the wage specified in its contract. The average wage paid must also be at least 115 percent of the average area wage, or 150 or 200 percent of the average area wage if the business contracted for the additional refund for salaries at those thresholds. The business will also receive a prorated refund if the local financial support received by OTTED is less than 20 percent of the refund authorized under the tax refund agreement.

**QTI Appropriations and Expenditures**

Since the inception of the QTI program, the tax refunds paid to QTI businesses have been less than the appropriations, resulting in significant reversions of appropriations. See Figure 1, below. The Auditor General initially addressed this issue in January 2001.[34] The disparity between appropriations and actual expenditures existed because OTTED did not know when preparing its legislative budget request how many businesses with which it contracted to pay tax refunds for job creation would actually submit claims for refunds. OTTED then requested, and the Legislature appropriated, enough funds to the QTI program to pay all possible tax refund claims. As a result, OTTED did not have to prorate tax refund claims as required by s. 288.095(3)(b), F.S. Many QTI businesses, however, did not submit claims for tax refunds because they did not meet the requirements of the QTI program, did not follow through with their business plans, or withdrew from participation in the program.




*Source:* Figure 1 is based on data supplied by the Senate Appropriations Subcommittee on Transportation and Economic Development.

One of the Auditor General recommendations was to change the program requirements for newly executed tax agreements to require businesses to submit tax refund requests by January of each fiscal year. In the agency's response to the Auditor General report, OTTED stated that it had already begun to require all new QTI projects to submit their tax refund claims by January 31.

[34] Auditor General, *Tax Refund Program for Qualified Target Industry Businesses Administered by the Executive Office of the Governor: Operational Audit,* Report No. 01-080, January 2001.

OTTED also emphasized that the change could only be applied to new QTI agreements, and, therefore, that it would take several years to realize the full benefit of the change.

In response to these findings and recommendations, the Legislature adopted ch. 2002-392, L.O.F., which modified the timeline for approval of QTI program refunds in order to improve the budgetary process for this appropriation. Tax refund claims were to be submitted by January 31 of each fiscal year for the jobs created by December 31. Refunds associated with those claims were to be paid out of the appropriation for the following fiscal year, thus providing an accurate estimate of the refund amount needed each fiscal year in time to be addressed during the appropriations process.

Although new contracts executed since this law change reflect the fixed claim date, the majority of pending claims are still based on contracts executed prior to the change. Therefore, the appropriation requests for FY 2002-03 and FY 2003-04 were still based primarily on projected refund claims. As a result, only $6.8 million of the total $24 million appropriation for FY 2002-03 was expended by June 30. Since there were pending contract payments on the balance of the appropriation, the Executive Office of the Governor approved the agency's request to certify forward $17.2 million, in accordance with s. 216.301, F.S. Of those funds, $8,429,114 was unspent on December 31, and therefore reverted to the Geveral Revenue Fund.

According to OTTED data reflecting contract dates, payment periods, and refund estimates, the transition to appropriation amounts based on actual claims payments is still many years away. The budget projection for FY 2004-05 totals $25.3 million based on a total of 241 estimated payments. Almost 70 percent of those estimated payments result from contracts entered prior to the fixed claim date, meaning that such claims can be submitted at any time during the fiscal year, assuming job goals are actually attained. Therefore, there is significant uncertainty regarding the actual cash needs for FY 2004-05. Further, it will be several years before the approved claims data will represent even the majority of the estimated payment amount, given that the last payments under the old contracts are still nine years away.

**QDC Program**

The qualified defense contractor (QDC) tax refund program was created in 1993 after the Cold War ended. The impetus for the program appears to have been Executive Order No. 93-118, signed by Governor Chiles on April 13, 1993.[35] The order found:

- The federal government is in the midst of major post-Cold War cuts in the nation's defense industry.
- By 1997, the federal defense budget is projected to decline by more than 42 percent, in real terms, from 1985 levels.
- The federal cuts include a 30-percent reduction in military personnel, base closures, and elimination of numerous defense contracts for goods and services, with employment losses in Florida of up to 55,000 by 1997.[36]

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[35] *See* Florida Senate Committee on International Trade, Economic Development, and Tourism, *Staff Analysis and Economic Impact Statement of CS/SB 32-C*, at 2-3 (Nov. 3, 1993).

Apparently, the QDC program was designed to help protect Florida defense businesses from cuts in federal defense spending.

The QDC program provides tax refunds for job creation similar to the tax refund program for qualified target industries.[37] The programs, however, differ significantly as follows:

- Tax refunds under the QDC program are paid for each job retained in addition to each new job created.[38]
- Participation in the QDC program is limited to certain defense contractors.[39]
- OTTED has the discretion to score applications for certification as a QDC business, and a tax refund of up to $5,000 per job is based on that score.[40]

**QTI and QDC Program Statistics**

According to the Enterprise Florida, Inc., (EFI) *2003 Incentives Report*, since the inception of the program in 1994 there have been 367 contracts with businesses under the QTI program.[41] Of these contracts, 322 are active contracts requiring QTI businesses to create 69,997 jobs with an average wage of $36,010 per job.[42] These businesses also proposed to make a total capital investment in this state of over $6.1 billion in their applications for certification as QTI businesses, which is an average investment of $23.94 for each dollar of tax refunds.[43] The average incentive per job for active QTI businesses is $3,641, according to EFI staff.[44]

Under the QDC program, there are two completed and two active contracts.[45] The active QDC businesses are contractually obligated to retain 350 jobs with an average salary of $53,472.[46]

Enterprise Florida, Inc., also conducts an economic impact analysis for the business operations proposed in each application for certification as a QTI or QDC business. To conduct the analysis, EFI uses an economic model based on the Regional Input-Output Modeling System (RIMS II) from the U.S. Department of Commerce.[47] The economic model is used to calculate the payback

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[36] Executive Order No. 93-118, Signed by Governor Lawton Chiles on April 13, 1993 (creating the Florida Defense Conversion Transition Commission).
[37] According to OTTED staff, the statute creating the QDC program was used as a model for s. 288.106, F.S., the statute creating the QTI program.
[38] OTTED authorizes the payment of tax refunds to QDC businesses for jobs retained. Section 288.1045, F.S., however, is ambiguous as to whether tax refunds are authorized for both retained and new jobs or only new jobs.
[39] Section 288.1045(3)(e)5., F.S.
[40] Section 288.1045(2)(b) and (3)(f), F.S.
[41] Enterprise Florida, Inc., *2003 Incentives Report: A Progress Report On Incentives Funded From the Economic Development Incentives Account*, November 2003, at 11.
[42] *Id.*
[43] *Id.*
[44] This figure does not include the value of other incentives in addition to the QTI incentives.
[45] *2003 Incentives Report, supra* note 41, at 14.
[46] *Id.*
[47] This economic model was designed by Rodney Peterson, a Ph.D. economist with the former Florida Department of Commerce, Bureau of Economic Analysis, circa 1995. This model may need to be revised to reflect changes in the state's tax code since the model's creation.

ratio to the state. The payback ratio is the amount of tax revenue returned to the state over a 10-year period for each dollar of tax refunds under the QTI and QDC programs. According to the model, the payback ratio to the state is $12.59 for the QTI program and $17.04 for the QDC program.[48]

## III. Effect of Proposed Changes:

This committee substitute implements the recommendations from *Review of Qualified Target Industry and Qualified Defense Contractor Tax Refund Programs* by the Senate Committee on Commerce, Economic Opportunities, and Consumer Services.[49]
In accordance with the recommendations in the report, the committee substitute provides that no additional businesses may be qualified to participate in the qualified target industry (QTI) and the qualified defense contractor (QDC) tax refund programs after June 30, 2009, thereby extending the programs for 5 years beyond their current scheduled closure date of June 30, 2004. The committee substitute also clarifies that tax refund agreements existing on June 30, 2009, continue in effect in accordance with their terms.

The committee substitute clarifies s. 288.1045, F.S., which creates the QDC program, to indicate that the program may be used to retain jobs. Applications for certification as a qualified defense contractor must also state the number of jobs to be retained.

Section 288.095, F.S., is amended by the committee substitute to require the Office of Tourism, Trade, and Economic Development (OTTED) to pay claims for tax refunds under both programs in the order approved. The committee substitute eliminates the requirements in current law requiring tax refund claims to be prorated if the Legislature does not appropriate sufficient funds to satisfy the amount of tax refund claims that OTTED estimates that it will receive. The committee substitute, however, authorizes the payment of refunds from the appropriation for the following fiscal year. By March 1 every year, OTTED must notify the legislative appropriations committees of any anticipated shortfall in the amount of funds needed to satisfy claims for tax refunds from the appropriation for the current fiscal year.

OTTED is directed by the committee substitute to attempt to amend existing tax refund agreements created under s. 288.106, F.S., the QTI program, to require tax refund claims to be submitted by January 31 for the net new full time equivalent Florida jobs as of December 31. Enterprise Florida, Inc., must report on OTTED's progress toward amending the tax refund agreements in its annual report on economic development programs. The report must also list the name and tax refund amount provided to each QTI and QDC business during the prior fiscal year.

The committee substitute takes effect upon becoming a law.

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[48] *2003 Incentives Report, supra* note 41, at 11 and 14. The amount of other state incentives also is included in the calculation of the payback ratio for the QTI program.
[49] Committee on Commerce, Economic Opportunities, and Consumer Services, The Florida Senate, Interim Project Report 2004-115, *Review of Qualified Target Industry and Qualified Defense Contractor Tax Refund Programs*, December 2003.

## IV. Constitutional Issues:

### A. Municipality/County Mandates Restrictions:

None.

### B. Public Records/Open Meetings Issues:

None.

### C. Trust Funds Restrictions:

None.

## V. Economic Impact and Fiscal Note:

### A. Tax/Fee Issues:

None.

### B. Private Sector Impact:

Because the committee substitute continues the existence of the qualified target industry and qualified defense contractor tax refund programs, additional businesses will be able to participate in the programs. Qualified target industry businesses that agree to amend the dates by which a tax refund claim must be submitted may incur costs to redetermine the dates by which jobs will be created.

### C. Government Sector Impact:

The Office of Tourism, Trade, and Economic Development (OTTED) is required to attempt to amend tax refund agreements to provide that claims for tax refunds are due before January 31 every year for jobs created as of December 31 of the preceding calendar year. OTTED may incur minimal administrative costs in its attempts to amend tax refund agreements. However, the change in the due date for tax refund claims will enable the Legislature to more accurately estimate the funds needed for tax refunds.

## VI. Technical Deficiencies:

None.

## VII. Related Issues:

None.

## VIII. Amendments:

None.