HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 293 Corporate Income Tax Credits

SPONSOR(S): Weatherford and others

TIED BILLS: **IDEN./SIM. BILLS:** SB 850

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Committee on Economic Development		West	Croom
2) Economic Expansion & Infrastructure Council			
3) Policy & Budget Council			
4)			
5)			

SUMMARY ANALYSIS

The program provides state tax credits for corporate income tax, under s. 220.11, F.S., and premium insurance tax, under s. 624.509, F.S., for qualified investments in Florida low-income communities.

The intent of HB 293 is to make the state more attractive to national investors who are deciding where to invest funds raised under the federal New Markets Tax Credits program by building a state "piggy-back" on tax credits offered by the federal program.

The credit provided under this bill is 8.33 percent per year for six years after the original date of the investment. Over six years this credit totals 50 percent of the investment. The federal program provides credits totaling 39 percent of the investment over a seven year period. A company with a qualified investment for both the federal and state program would receive 89 percent of the purchase price of the investment in tax credits**.** Any amount of the tax credit may be carried forward for future taxable years, however all tax credits expire December 31, 2029. The tax credits are allocated on a first-come, first-serve basis.

A total of $105 million in tax credits may be awarded for the duration of the program with no more than $15 million claimed in each state fiscal year. The annual limit of $15 million in tax credits claimed does not include credits carried forward from previous tax years.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

Provide Limited Government: This bill grants separate rule-making authority to the Department of Revenue (DOR) and the Office of Tourism, Trade, and Economic Development (OTTED) for the purpose of administering the provisions set out in this bill including the recapture provision and the allocation of tax credits issued for qualified equity investments and recapture of these credits.

Ensure Lower Taxes: This bill provides tax credits to entities making investments in low-income communities in Florida.

B. EFFECT OF PROPOSED CHANGES:

Present Situation:

Certified Capital Companies

Currently, Florida offers direct tax credits for premium insurance tax through the Certified Capital Company Act (CAPCO).

The 1998 Florida Legislature enacted the Certified Capital Company Act[1] to encourage private investment in venture capital by providing direct tax credits for investment in qualified businesses. The stated purpose of this act is to stimulate a substantial increase in venture capital investments in Florida by providing an incentive for insurance companies to invest in state-certified capital companies (CAPCOs) which, in turn, will invest in new or expanding businesses.[2] Eligible insurance companies are granted insurance premium tax credits in amounts equal to investments in CAPCOs. The increase in investment capital is intended to contribute to employment growth, create high-paying jobs, and expand or diversify Florida's economy.

To date, the insurance industry has invested $150 million in three state-certified CAPCOs. The insurance companies may claim insurance premium tax credits totaling $15 million each year for ten years.

According to information in the most recent annual OPPAGA report on the CAPCO program, there were 47 qualified businesses in which the CAPCOs had invested as of December 31, 2004.[3] Examples of industries represented by the qualified businesses are electronic imaging, medical technology, boat manufacturing, credit card payment processing, vehicle fleet management systems, an internet portal for fishermen, and a cookie manufacturer. The most recent investments include businesses predominantly in the child daycare, landscaping, and restaurant industries. The total number of full-time jobs in qualified businesses at the time of the initial investments in the 47 companies was 1,218. The total number of full-time jobs in all qualified businesses as of December 31, 2004 was 1,009.

[1] Section 288.99, F.S
[2] Section 288.99(2), F.S.
[3] Section 288.99(12), F.S., requires OTTED to report annually on the performance of the CAPCO program. The following Information was compiled from the latest annual report issued in 2004. Executive Office of the Governor, Office of Tourism, Trade & Economic Development, *Certified Capital Company Act Annual Report on Performance*, June 2005.

While as many as nine states have created CAPCOs, this type of program is increasingly viewed by researchers as the more "problematic" of the Venture Capital Funds (VCF) programs, in terms of

> "…its high cost, poor design and target-inefficiency. Unlike any other VCF program, the CAPCO program provides a 100% premium tax credit to insurance company investors. In effect, the government underwrites the entire investment risk."[4]

Federal New Markets Tax Credit

The New Markets Tax Credit Program permits taxpayers to receive a credit against federal income taxes for making qualified equity investments in designated Community Development Entities (CDEs). The CDE must in turn invest the qualified equity investments in low-income communities. The credit provided to the investor totals 39 percent of the cost of the investment and is claimed over a seven-year period. In each of the first three years, the investor receives a credit equal to five percent of the total amount paid for the stock or capital interest at the time of purchase. For the final four years, the value of the credit is six percent annually. Investors may not realize a return on their investments in CDEs prior to the conclusion of the seven-year period.[5]

An organization wishing to receive awards under the NMTC Program must be certified as a CDE by the US Department of Treasury.

To qualify as a CDE, an organization must:
- Be a domestic corporation or partnership at the time of the certification application;
- Demonstrate a primary a mission of serving, or providing investment capital for, low-income communities or low-income persons; and
- Maintain accountability to residents of low-income communities through representation on a governing board of or advisory board to the entity.[6]

Community Development Entities in Florida, Investment by State

There are 56 CDEs in Florida.[7] Florida trails only New York (121), California (116), Texas (66), Pennsylvania (59), and Illinois (58) in total number of CDEs.[8] The federal program has awarded New Markets Tax Credits to at least 179 CDEs nationwide; these CDEs would be eligible to utilize the state program created in this bill.[9]

Under the federal program, loans have been used to finance a range of activities, such as the rehabilitation of historic buildings and the operation of mixed-use real estate development. Other uses include the construction or operation of cultural arts centers, frozen pizza manufacturing, and the construction of daycare centers and charter schools. [10]

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[4] Statement of Professor Daniel Sandler, University of Western Ontario, London; senior research fellow of the Taxation Law and Policy Research Institute, Melbourne; associated with Minden Gross Grafstein & Greenstein LLP, Toronto. See Daniel Sandler, *Venture Capital and Tax Incentives: A Comparative Study of Canada and the United States* (Toronto: Canadian Tax Foundation, 2004).
[5] Community Development Financial Institutes Fund; the Department of Treasury; information contained in this paragraph can be found at http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5 (visited 3/15/07).
[6] Community Development Financial Institutes Fund; the Department of Treasury; available online at http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5 (visited 3/15/07).
[7] Community Development Financial Institutes Fund; the Department of Treasury; available online at http://www.cdfifund.gov/docs/certification/CDEstate.pdf .
[8] Id.
[9] United States Government Accounting Office (GAO) *Report to Congressional Committees, Tax Policy, January, 2007, page 15.*
[10] Id at *30.*

Florida ranked 25th in total NMTC investment dollars during fiscal years 2003-2005. The state received 1.23 percent of total loans and investments and eight total projects.[11]

State	Total dollar amount of loans and investment	Percentage of all loans and investment	Number of NMTC projects	Percentage of NMTC projects
1.California	$303,081,270	9.74	58	9.95
2. New York	239,178,566	7.68	25	4.29
3. Ohio	201,857,969	6.49	69	11.84
4. Maine	153,527,250	4.93	13	2.23
5. Wisconsin	149,131,108	4.79	26	4.46
6. Missouri	146,165,868	4.70	22	3.77
7. Massachusetts	145,059,237	4.66	34	5.83
8. Kentucky	135,117,406	4.34	44	7.55
9. North Carolina	126,420,590	4.06	14	2.40
10. Washington	125,703,680	4.04	19	3.26
11. Minnesota	122,587,357	3.94	13	2.23
12. Oklahoma	112,092,186	3.60	24	4.12
13. Oregon	111,464,317	3.58	14	2.40
14. Maryland	106,171,382	3.41	14	2.40
15. New Jersey	83,439,000	2.68	7	1.20
16. Pennsylvania	77,111,177	2.48	21	3.60
17. Arizona	68,476,055	2.20	8	1.37
18. Washington D.C.	67,715,807	2.18	10	1.72
19. Texas	65,644,265	2.11	11	1.89
20. Michigan	57,541,869	1.85	10	1.72
21. Virginia	55,898,873	1.80	8	1.37
22. Rhode Island	55,235,675	1.77	3	0.51
23. Utah	53,884,716	1.73	14	2.40
24. Georgia	38,516,906	1.24	4	0.69
25. Florida	***38,261,093***	***1.23***	***8***	***1.37***

Effects of Proposed Changes:

HB 293 creates the Florida New Markets Tax Credit in s. 288.991, F.S. The program will provide state tax credits for corporate income tax, under s. 220.11, F.S., and premium insurance tax, under s. 624.509, F.S., for qualified investments in Florida low-income communities.

The intent of the bill is to “piggy-back” on tax credits offered by the federal New Markets Tax Credit Program to provide greater investment in Florida.

How the Program Works

Under this program, federally-certified CDE’s, which have entered into allocation agreements with the U.S. Treasury, have the ability to apply to the Office of Tourism Trade and Economic Development (OTTED) for a certification of Florida tax credits. The CDE must show that they are prepared to invest a certain amount of capital into qualified businesses in Florida’s low-income communities. The certification process would include proof of the CDEs eligibility, identification of its investors, description of the investments to be raised by the CDE, information regarding the proposed low-income community investments, a description of the CDEs efforts to partner with local community-based groups, and a non-refundable $1,000 application fee. OTTED will also be able to request additional information deemed necessary. OTTED will certify qualified applications on a first-come, first-serve basis.

[11] Information found in the table came from the United States Government Accounting Office (GAO) *Report to Congressional Committees, Tax Policy, January, 2007.*

Once OTTED certifies a CDEs qualified equity investment, the CDE has 30 days to raise its investment capital (the qualified equity investment) and then 12 months to make the investment in a low-income community. Thereafter, the CDE must annually report to OTTED information, including a list of low-income community investments and the amount of the investments with third-party proof that the investment was made. Any CDE that is allocated more than $500,000 in tax credits in any state fiscal year will also be required to participate in Florida's Single Audit program. Any failure by a CDE to follow either Florida or federal law may result in the state recapturing tax credits claimed, together with interest and penalties.

Qualified Investments

A "qualified equity investment" means any equity investment or long-term debt security by a qualified CDE that:

- Is acquired on or after July 1, 2008;
- Has at least 85 percent of its cash purchase priced invested in a qualified low-income community investments; and
- Is designated by the CDE as a qualified equity investment, regardless whether the investment was designated under the federal New Markets Tax Credit Program.

In addition, a qualified equity investment may mean an equity investment or long-term debt security that is currently a qualified equity investment.

The definition for a "qualified equity investment" in this bill expands the federal definition allowed under Sec. 45D of the Internal Revenue Code. It allows a CDE to designate a qualified investment regardless of whether it is allowed under the federal program; and it allows for long-term debt security to be a qualified investment.

"Long-term debt security" means any debt instrument issued by a CDE, "at par value or a premium, having an original maturity date of at least seven years following the date of its issuance, with no acceleration of repayment, amortization, or prepayment features before its original maturity date, and having no distribution, payment, or interest features related to the profitability of the qualified community development entity or performance of the qualified community development entity's investment portfolio."

Qualified Active Low-Income Community Business

A "qualified active low-income community business" is defined as having the same meaning as what is provided in federal law. It also includes language different from federal law that states the business must not derive 15 percent or more of its annual revenue from the rental or sale of real estate. Businesses such as golf courses, country clubs, massage parlors, tanning salons, liquor stores, and establishments that permit gambling are not eligible for this program.

A low-income community is defined as any population census tract within the state for which the federal individual poverty rate of such tract is at least 20 percent. For census tracts not located within a metropolitan area to qualify as a low-income community, the median family income must not exceed 80 percent of the statewide median income. For census tracts located within a metropolitan area, the median family income must not exceed 80 percent of the greater of statewide median family income or the metropolitan area median income.

Tax Credits

The bill allows a tax credit to be taken annually only after the investment has been made and held for a full year. The credit provided under this bill is 8.33 percent per year for six years after the originally date of the investment. Over six years this credit totals 50 percent of the investment. Any unused portion of the tax credit may be carried forward for future taxable years; however, all tax credits expire on December 31, 2029. No more than $15 million in tax credits may be claimed in any fiscal year. The amount of investments that may be used to calculate a CDE's tax credit is capped at $10 million annually.

The federal program provides credits totaling 39 percent of the investment over a seven year period. A company with a qualified investment for both the federal and state program would receive 89 percent of the purchase price of the investment in tax credits**.**

A business would qualify for credits as follows:

Year	State Program	Federal Program
1	0%	5%
2	8.33%	5%
3	8.33%	5%
4	8.33%	6%
5	8.33%	6%
6	8.33%	6%
7	8.33%	6%
Total	**49.98%**	**39%**

OTTED certifies an investment to the Department of Revenue (DOR). The CDE is required to provide DOR the anticipated dollar amount of an investment in the state during the first 12-month period following the initial credit allowance date. DOR is required to adjust future credits if the actual amount of the investment is different from the estimated amount.

The bill does not allow the transfer or sale of tax credits, but does allow a tax credit to travel with the purchase of an investment to a new owner.

Any investor that receives an annual allocation of tax credits that exceeds $500,000 shall be treated as a recipient pursuant to s. 215.97(2), F.S., and required to participate in a state single audit pursuant to the provisions of s. 215.97, F.S.

The department shall recapture tax credits available to an investor if:

- For any reason the federal government recaptures a related tax credit;
- The CDE redeems any principal repayment related to the investment prior to its seventh anniversary;
- The requirement to maintain at least 85 percent of the investment in low-income community investments in Florida is not met;
- The CDE fails to provide to OTTED and DOR any of the information or reports required by this bill; or
- A taxpayer received credits to which they were not entitled.

The bill gives DOR and OTTED the authority to adopt rules pursuant to ss. 120.536(1) and 120.54, F.S., to implement the provisions of this bill. OTTED must submit an annual report each July 1, beginning in 2010 to the Governor, the President of the Senate, and the Speaker of the House of Representatives detailing all qualified low-income community investments made in Florida, their location, the total dollar amount invested, the number of jobs created or retained, and the value of applicable tax credits claimed for the most recent year.

C. SECTION DIRECTORY:

Section 1 - Creates s. 288.991, F.S., the New Markets Tax Credit.

Section 2 - Amends subsection (8) of s. 220.02, F.S., to provide legislative intent for the application of tax credits.

Section 3 - Amends paragraph (a) of subsection (1) of s. 220.13, F.S., to define “adjusted federal income” and provide additions to taxable income.

Section 4 - Creates subsection (19) of s. 213.053, F.S., to allow DOR to share information with OTTED and to provide confidentiality to taxpayers utilizing the program created by this bill.

Section 5 - Provides an effective date of July 1, 2008 and provides that the program created by this bill applies to tax years ending after December 31, 2008.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   See “Fiscal Comments”.

2. Expenditures:

   See “Fiscal Comments”.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

   None.

2. Expenditures:

   None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Investments may assist existing and new businesses.

D. FISCAL COMMENTS:

Over seven years, the total fiscal impact of the program is limited to $105 million in tax credits. The bill further limits the amount of tax credits claimed each year to $15 million plus any unused credits that have been carried forward. If CDEs carry forward a substantial amount of unused credits and claim them in a single year, there is no guarantee that the amount of credits claimed in any year, besides year two of the program, would be $15 million or less.[12]

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

This bill does not require counties or municipalities to spend funds or take action requiring the expenditure of funds. This bill does not reduce the percentage of state tax shared with counties or municipalities. This bill does not reduce the authority that municipalities have to raise revenue.

2. Other:

B. RULE-MAKING AUTHORITY:

This bill grants separate rule-making authority to DOR and OTTED for the purpose of administering the provisions set out by this bill including the recapture provision and the allocation of tax credits issued for qualified equity investments.

C. DRAFTING ISSUES OR OTHER COMMENTS:

DOR performed an analysis of this bill and recommended deleting the tax credit election language in lines 273 through 282 (288.991(3)(f)). The section requires a CDE to elect the type of tax liability to apply its earned credit against. Insurers are required to apply an earned credit against their insurance premium tax liability so they have no choice of how to apply their tax credit.

D. STATEMENT OF THE SPONSOR:

No statement submitted.

IV. AMENDMENTS/COUNCIL SUBSTITUTE CHANGES

[12] Year two of the program created by this bill is the first year in which tax credits may be claimed by a CDE.