HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/HB 1487 Insurance Premium and Corporate Income Tax Credits
SPONSOR(S): Economic Expansion & Infrastructure Council; Rep. Schenck
TIED BILLS: **IDEN./SIM. BILLS:** SB 2280

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Committee on Economic Development	7 Y, 0 N	West	Croom
2) Economic Expansion & Infrastructure Council	14 Y, 0 N, As CS	West	Tinker
3) Policy & Budget Council			
4)			
5)			

SUMMARY ANALYSIS

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 CS provides that the program is contingent on funds (sufficient to offset the tax credits) being appropriated from the General Revenue Fund for that fiscal year. Should the budget provide adequate appropriations, no more than $15 million in tax credits may be issued in any fiscal year.

The intent of CS/HB 1487 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. Florida ranked 25th in total NMTC investment dollars during fiscal years 2003-2005.

The credit provided under this CS 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, 2028. The tax credits are allocated on a first-come, first-serve basis.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

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

Ensure Lower Taxes: This CS provides tax credits to companies or 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] This program encourages 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.

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

[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.

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 CS.[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 charter schools. [10]

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]

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

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:

CS/HB 1487 creates the Florida new markets development program in ss. 288.991 and 288.992, 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 CS 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 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.

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, 2007;
- 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 CS 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 7 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 CS 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 CS 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, 2028. The CS provides that the program is contingent on funds (sufficient to offset the tax credits) being appropriated from the General Revenue Fund for that fiscal year. Should the budget provide adequate appropriations, no more than $15 million in tax credits may be issued in any fiscal year.

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%**

The Office of Tourism, Trade, and economic Development (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 CS 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.

The maximum amount of tax credits allocated in any year shall not exceed $15 million. However, the CS provides that the program is subject to appropriation.

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 CS; or
- A taxpayer received credits to which they were not entitled.

The CS 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 CS.

C. SECTION DIRECTORY:

Section 1 - Creates ss. 288.991 and 288.992, F.S., the New Markets Tax Credit Act.

Section 2 - Creates subsection (19) to s. 213.053, F.S., to allow DOR to share certain information with OTTED.

Section 3 - Amends subsection (8) of s. 220.02, F.S., to provide legislative intent for the application of tax credits.

Section 4 - Amends paragraph (a) of subsection (1) of s. 220.13, F.S., to include a provision for a qualified equity investment.

Section 5 - Provides an effective date of July 1, 2007.

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:

The CS provides that the program is contingent on funds (sufficient to offset the tax credits) being appropriated from the General Revenue Fund for that fiscal year. Should the budget provide adequate appropriations, no more than $15 million in tax credits may be issued in any fiscal year. Over seven years, the total fiscal impact of the program could be $105 million in tax credits.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

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

2. Other:

B. RULE-MAKING AUTHORITY:

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

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

D. STATEMENT OF THE SPONSOR

Florida has drastically under-participated in Federal New Markets Tax Credit Program, the $20 billion federal economic development program which encourages investment in low-income areas throughout the nation. Currently our state ranks 25th in the country in new markets investments. To date, over half of that money is still waiting to be invested and less than 1.5% has been invested in our state. Other states offering tax credits which investors can "piggyback" with the federal credits outperform Florida in attracting new markets investment dollars by as much as a 8:1 ratio. In fact, qualified entities located in Florida appear to be making their investments in other states.

The intent of this legislation is to leverage the federal program to bring investment to Florida's rural and urban low income communities by adding a state investment in the form of a state tax credit. Economic Data suggests this program if fully utilized would create jobs in Florida's poorest communities and attract up to $540 million of development capital to rural and urban areas with a maximum $15 million annual cost to the state and a maximum total cost of $105 million over 7 years. Specifically, incentives would only be used if investments are made. The leveraging of these types of investments to bring in other sources of capital typically produces a positive impact of 10-20 times the value of the incentives. Further, credits would only be available to those entities that are certified through the Department of Treasury as eligible for federal tax credits through thorough the Federal New Markets Tax Credit Program. Therefore, the program can be administered and monitored with minimal state resources. In fact, Florida would have the protection of a 7 year federal claw-back provision, ensuring that the investments are made and kept in the targeted communities.

The goal is for Florida to get a larger share of the New Markets investments made nationwide. The Florida New Markets Development Program intends to make the state more attractive to national investors who are deciding where to invest funds raised under the federal New Market Tax Credits program.

IV. AMENDMENTS/COUNCIL SUBSTITUTE CHANGES

On Tuesday March 30, 2007, The Committee on Economic Development reported the bill favorably with one amendment. The amendment:

- Allows DOR to allocate tax credits of up to $15 million per fiscal year and any credits not awarded or any credits that are forfeited shall be available in subsequent fiscal years;

- Requires the taxpayer to provide audited financial statements to DOR and make an irrevocable decision at the time when the qualified equity investment is made to apply the tax credit to tax liabilities set out in chapter 220 or chapter 624 or a combination of both. The decision will be binding on any subsequent holder of the credit;

- Adds language to specify the right of DOR to revoke tax credits that are not applied in a lawful manner. Any applicant that submits a fraudulent application will be penalized double the amount of the credit and that applicant will be liable for any costs associated with processing a fraudulent claim; and

- Provides a repeal date of July 14, 2014, except for tax credits that are carried forward as specified.

On Friday April 20, 2007, The Economic Expansion and Infrastructure reported the bill favorably with a council substitute. The council substitute:

- Creates the program in statute;
- Allows DOR and OTTED to provide oversight to the program;
- Incorporates the federal definition for low-income community;
- Provides an expiration date for tax credits that are carried forward over taxable years;
- Provides the order (first-come-first-serve) in which tax credits may be claimed;
- Provides an add-back to the amount of credit against corporate income tax;
- Provides that tax credits are subject to annual appropriations;
- Grants separate rule-making authority to DOR and OTTED; and
- Provides a sunset and repeal of the statute created for this program.