The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

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

Prepared By: The Professional Staff of the Finance and Tax Committee

BILL: SB 2426

INTRODUCER: Senator Fasano

SUBJECT: New Markets Development Program

DATE: April 9, 2010 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Pugh	Cooper	CM	**Favorable**
2.	Wolfgang	Yeatman	CA	**Fav/1 amendment**
3.	ODonnell	McKee	FT	**Favorable**
4.			WPSC	
5.				
6.				

Please see Section VIII. for Additional Information:

A. COMMITTEE SUBSTITUTE..... [ ] Statement of Substantial Changes

B. AMENDMENTS........................ [ ] Technical amendments were recommended

[x] Amendments were recommended

[ ] Significant amendments were recommended

I. Summary:

The Legislature in 2009 created the "Florida New Markets Development Program" (NMDP) to provide state tax credits for certain types of investments in low-income communities.[1] Investors in Florida NMDP projects can recapture up to 39 percent of their investments as a credit against state corporate or premium insurance taxes. The cap on the Florida tax credits is $97.5 million over 7 years, with up to $20 million available each year. Credits can be claimed against taxes owed beginning in FY 2011-2012. The program expires in 2022.

SB 2426 changes two provisions in the state definition of "qualified active low-income community business" (qualified business) to be consistent with the federal New Markets Tax Credit (NMTC) program. Briefly:

- It allows a business to qualify for the state program even if it does not derive at least 50 percent of its total gross income from business activities in a low-income community if it uses at least 50 percent of its tangible property within a low-income community <u>or</u> if at least 50 percent of its services are performed through its employees in a low-income community;

[1] Part XIII of ch. 288, F.S. Created by ch. 2009-50, L.O.F. (CS/CS/HB 485).

- It defines "substantial percentage" as used in the definition for qualified active low-income community business as 40 percent; and
- It amends the provision preventing a qualified business from deriving or projecting to derive 15 percent or more of its annual revenue from the rental or sale of real estate, by allowing the percentage cap to be pierced only if the qualified business is leasing property to another qualified business that is an affiliated company.

The Revenue Estimating Conference has determined that the bill has no impact on state and local revenue.

SB 2426 substantially amends s. 288.9913, F.S.

II. Present Situation:

The Federal New Market Tax Credit Program

Created in 2000, the New Markets Tax Credit Program[2] (NMTC) permits taxpayers to receive a credit against federal income taxes for making qualified equity investments in designated Community Development Entities (CDE's). Substantially all of the qualified equity investment must in turn be used by a CDE to provide loans or capitalization projects in "low-income communities." CDE's are certified by the U.S. Treasury Department and receive an allocation of federal income tax credits. The CDE's use these allocated tax credits to attract investors, and award the credits to their investors after receiving the investments.

The federal credits provided to an investor may total 39 percent of the investment and is claimed over a 7-year credit allowance period. In each of the first 3 years, the investor receives a credit equal to 5 percent of the total amount paid for the stock or capital interest at the time of purchase. For the final 4 years, the value of the credit is 6 percent annually. Investors may not redeem their investments in CDE's prior to the conclusion of the 7-year period.

For purposes of the federal law, "low-income communities" are U.S. census tracts where:

- There is a documented minimum 20-percent poverty rate;
- The median family income does not exceed 80 percent of the area median family income;
- A population of less than 2,000, are contained within a federally designated Empowerment Zone, and are contiguous to at least one other low-income community; or
- The median family income does not exceed 85 percent of the area median family income, provided the census tract is located in a high-migration rural county.

The IRS and the U.S. Treasury Department's Community Development Financial Institutions Fund (CDFI) are responsible for monitoring the program. Implementation of the NMTC program is guided by the law that created it (the Community Renewal Tax Relief Act – PL 106-554), various administrative rules adopted by the IRS, and interpretive policy letters issued by IRS and CDFI.

[2] Internal Revenue Code 26 C.F.R. § 45D (2005).

Since the inception of the New Markets program, the CDFI has awarded $26 billion to qualified CDE's – the total amount of tax credits authorized by Congress.[3] In the first six rounds of the federal tax credit allocations, CDE's whose service areas include Florida have received cumulative federal income tax credit allocations of at least $2.2 billion. In 2008, the most recent figures available, eight CDE's whose territories of operation include Florida (but who are not headquartered in Florida) received $468.25 million in tax credit allocations.[4]

Over the life of the program, it appears that only one CDE based in Florida – the Florida Community Loan Fund – has ever received an allocation of federal New Markets tax credits, and that was in 2003.[5] According to its executive director, the Florida Community Loan Fund used some of its New Market credits to attract investors to a charter school development project in Miami.[6] It currently is involved in the development of an 118,000-square-foot research and development building at the University of Miami Life Sciences Park for use by early-stage bioscience companies.

As of 2007, there were 63 CDE's with service areas in Florida,[7] trailing only New York (121), California (116), and Texas (66). Nationally, there are 2,223 federally certified CDE's. A GIS map prepared using data maintained by the U.S. Treasury's Community Development Financial Institutions Fund indicates areas within nearly two dozen Florida counties that are New Market Tax Credit Qualified Tracts, because they meet the low-income and other federal requirements.

A 2010 analysis of the federal NMTC program by the U.S. Government Accountability Office[8] indicated that 65 percent of CDE investments have been made in real-estate projects; 22 percent to finance business-related activities (such as purchases of fixed assets or investments in a particular business); 11 percent for mixed purposes; and 1 percent for other uses.[9]

The federal New Markets Tax Credit Program expired December 31, 2009, but there are at least two bills to extend it: H.R. 4213, a large tax-related bill that must go back to the U.S. House for agreement with U.S. Senate amendments, and SB 1831, which remains in committee.

Examples of New Markets projects in other states

At least two states – Louisiana and Illinois – have enacted state New Markets programs that piggyback the federal program. But federal New Markets investments have been made in nearly all 50 states.

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[3] GOVERNMENT ACCOUNTABILITY OFFICE, THE NEW MARKETS TAX CREDIT: THE CREDIT HELPS FUND A VARIETY OF PROJECTS IN LOW-INCOME COMMUNITIES, BUT COULD BE SIMPLIFIED 4 (Jan. 2010) *available at* http://www.gao.gov/new.items/d10334.pdf.

[4] http://www.cdfifund.gov/docs/2008/nmtc/2008NMTCStatesServed.pdf. Site under reconstruction as of March 15, 2010.

[5] Florida Community Loan Fund, Inc., received $15 million in federal NMTC, according to the http://www.cdfifund.gov/awardees/db/basicSearchResults.asp. Site under reconstruction as of March 15, 2010.

[6] Information derived from email and telephone interviews with FCLF executive director Ignacio Esteban, occurring variously within March 4-March 12, 2009. Documents on file with the Commerce Committee.

[7] Available online at http://www.cdfifund.gov/awardees. Site under reconstruction as of March 15, 2010.

[8] GOVERNMENT ACCOUNTABILITY OFFICE, THE NEW MARKETS TAX CREDIT: THE CREDIT HELPS FUND A VARIETY OF PROJECTS IN LOW-INCOME COMMUNITIES, BUT COULD BE SIMPLIFIED n. 4, 11-13 (Jan. 2010) *available at* http://www.gao.gov/new.items/d10334.pdf.

[9] *Id.*

Examples of the types of projects include:[10]

- Expansion of a pet-food manufacturer in Red Bay, Alabama, that created 200 jobs.
- Development of the National Hispanic University in a low-income area of San Diego.
- Improvements to a tortilla bakery operation in Haywood, California, creating five jobs.
- Building and equipment purchases in Marion, Indiana, to rejuvenate a paper-products company, creating 40 jobs.
- Investment in a mixed-use Life Sciences Park in Baltimore, near Johns Hopkins Hospital, designed to include scientific laboratories, residential units, and retail stores.
- Expansion of a women's sleepwear manufacturer in McAlester, Oklahoma, creating 70 jobs.
- Improvements to a wheat processing mill in a north Texas community that was used by a multi-state farmers' cooperative, and refinancing of the mill's existing debt.
- Restoration of an historic hotel in Seattle into a museum and government offices, as part of a larger redevelopment project for the neighborhood.

Florida's New Markets program

The state's NMDP is based in large part on the federal program, sharing many of the definitions, requirements, and basic investment processes for receiving and investing investor credits. The reason for this was to make it easy for investors to "piggyback" their investments in projects that would qualify for both federal and state tax credits, meaning up to 78 percent of their investment is available to reduce their tax liabilities.

Briefly, the NMDP works this way:[11]

- One or more qualified CDE's will attract private investors, typically large banks or insurers, to invest in proposed business development projects in low-income communities.
- The CDE's then will apply to the Governor's Office of Tourism, Trade, and Economic Development (OTTED) for its approval to make qualified investments in eligible businesses within low-income communities, using the funds raised in exchange for the corporate income or insurance premium tax credits.
- Once notified by OTTED, the state Department of Revenue (DOR) will begin tracking tax credit claims from the CDE investors.
- Credits may not be claimed until 2 years after the qualified investments were made. So, in the third year of the program, up to $17.5 million in tax credits may be claimed, and in each of the subsequent 4 years, $20 million in new credits may be claimed against taxes owed.

In Florida law, a "qualified active low-income community business" (qualified business) is a corporation or partnership that must meet the following criteria:

- It must derive at least 50 percent of its total gross income each taxable year from its business activities within the low-income community, use a "substantial portion" of its tangible property within the low-income community in any taxable year, and provide

[10] Examples from across the nation are described in a New Markets Tax Credit Coalition report at http://nmtccoalition.org/wp-content/uploads/2009/10/50-Projects-50-States-Report.pdf. Last visited March 12, 2010.

[11] A detailed explanation of the Florida NMDP is in the 2009 bill analysis of CS/CS/SB 1502, available at http://www.flsenate.gov/data/session/2009/Senate/bills/analysis/pdf/2009s1502.wpsc.pdf. Last visited March 8, 2010.

a "substantial portion" of its services (meaning employee wages) within the low-income community.

- It must create or retain jobs that pay an average wage of at least 115 percent of the federal poverty wage for a family of four.
- It must not derive 15 percent or more of their annual revenue from the rental or sale of real estate; engage "predominantly" in the development or holding of intangibles for sale or licenses; operate a private or commercial golf course, country club, massage parlor, hot-tub facility, suntan facility, race track or other facility used for gambling, or a store whose principle business is the sale of alcoholic beverages for consumption off premises; or be principally involved in farming, if the sum of the aggregate unadjusted bases or the fair market value of the assets owned by the business, and the aggregate value of its leased assets exceeds $500,000.
- It must provide the CDE with reasonable expectation that it will meet the above requirements.

OTTED has approved six CDE applications and awarded the CDE's $72.486 million in New Markets tax credits.[12] The CDE's have proposed total qualified investments in the amount of $162.4 million. Specific information is in the chart below.

Applicant	Qualified Investment Proposed	Tax Credits Approved by OTTED
Capital Trust Agency Community Development Entity	$10 million	$3.9 million
BizCapital BIDCO II	$12.4 million	$4.836 million
Florida Community Development I	$50 million	$19.5 million
Florida Community Development II	$15 million	$5.85 million
Stonehenge Community Development	$25 million	$9.75 million
Stonehenge Community Development	$50 million	$19.5 million
Total	**$162.4 million**	**$63.336 million**

According to OTTED, the CDEs are continuing their fund-raising and evaluation efforts, and have made no investments in qualified businesses to date. About $34.2 million in NMDP credits remain to be awarded by OTTED over the life of the program.

III. Effect of Proposed Changes:

Section 1 amends s. 288.9913, F.S., to substantially modify the definition of a "qualified active low-income community business" (qualified business) to make it consistent with current federal policy.

The bill modifies two of the four criteria that a business must meet in order to be qualified under Florida's NMTC program: its level of activity within a low-income community and the types of activities it cannot engage in.

[12] Based on January 15, 2010, email from, and subsequent conversations with, OTTED staff. On file with the Commerce Committee.

First, the qualified business would have to use at least 40 percent (rather than "a substantial portion") of its tangible property within any low-income community for any taxable year and perform at least 40 percent (rather than a "substantial portion") of its services through its employees in a low-income community for any taxable year. The basic formula for determining the percentage is to divide the average value of the tangible property (or amount of wages paid to employees) used in the low-income community by the business' average total value of tangible property (or total wages paid).

Additionally, a qualified business that uses at least 50 percent of its tangible property and performs at least 50 percent of its services through its employees is assumed to be in compliance with one of the other requirements – that it derives at least 50 percent of its total gross income from the active conduct of business within a low-income community during any taxable year. The second modified criterion specifies the conditions under which a qualified business may, in fact, derive 15 percent or more of its annual revenue from the rental or sale of real estate, if the primary lessee and user of the property is another qualified business that is either owned or controlled by, or is under common ownership or control with, the lessor.

These changes to the definition of qualified business must be made statutorily, and not through OTTED via the ch. 120, F.S., rulemaking process – as supporters of the original 2009 legislation thought.[13]

Section 2 provides that this act takes effect upon becoming law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

The Revenue Estimating Conference has determined that the bill has no impact on state and local revenue.

[13] March 10, 2010, conversation with Tony Toups and Slater Bayless, representing Advantage Capital Partners.

B. Private Sector Impact:

Indeterminate. Supporters of the legislation say this change will make the Florida New Markets tax credit program more attractive to potential investors and to new or existing businesses in low-income communities.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:

A. Committee Substitute – Statement of Substantial Changes:
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

Barcode 376286 by Community Affairs on April 7, 2010:
Aligns s. 288.9920, F.S., to set the same "cure period" used in the federal regulations (68 C.F.R. 248 (Dec. 28, 2004)). This provision allows qualified equity investments that fail to meet the federal requirements to correct the failure within 6 months. Only one correction is permitted for each investment during the seven year credit period.