

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 943 Capital Formation for Infrastructure Projects

**SPONSOR(S):** Eisnaugle and others

**TIED BILLS:** **IDEN./SIM. BILLS:** SB 976

| REFERENCE   | ACTION    | ANALYST | STAFF DIRECTOR or<br>BUDGET/POLICY CHIEF |
|---|-----------|---------|--|
| 1) Economic Development & Tourism<br>Subcommittee | 14 Y, 0 N | Tecler  | Kruse                                    |
| 2) Finance & Tax Committee                        | 20 Y, 2 N | Wilson  | Langston                                 |
| 3) Economic Affairs Committee                     |           |         |  |

### SUMMARY ANALYSIS

HB 943 creates the Florida Infrastructure Fund Partnership ("Partnership"), a contingent tax credit program designed to leverage investment and private funding for state infrastructure projects, which may encourage private sector economic activity. The Partnership is authorized to raise \$700 million in private funds for direct investment in infrastructure projects including water or wastewater systems, communication systems, power systems, transportation systems, renewable energy systems, ancillary or support systems, or other strategic infrastructure needs. Tax credits are available for redemption no earlier than 2023 and will be used only as a guarantee on an investment partner's principal investment. The Florida Opportunity Fund will serve as the general partner of the program. A separate entity, the Florida Infrastructure Investment Trust will administer the tax credit program.

The Revenue Estimating Conference estimated that the bill will have a recurring negative indeterminate impact on both state and local government revenues, possibly beginning in 2023, due to contingent tax credits. No more than \$150 million in credits may be utilized in any one state fiscal year.

The bill provides for an effective date of July 1, 2011.

# FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

### A. EFFECT OF PROPOSED CHANGES:

#### Issue Background

##### **The Florida Opportunity Fund**

The Florida Opportunity Fund, Inc. ("Fund") was created by the Florida Legislature in 2007 to mobilize and increase venture capital available to Florida businesses. Sections 288.9621 - 288.9625 F.S., collectively referred to as the Florida Capital Formation Act, provided for the authorization of the entity. Initially, the Fund was set up as a "fund-of-funds" program that emphasized investment in seed capital and early stage venture capital funds. However in 2009, the Florida Legislature expanded the Fund's directive under the Florida Capital Formation Act to create direct investment programs that invest in individual businesses and infrastructure projects. The fund may not use its original appropriation of \$29.5 million to make direct investments but may raise private capital or utilize other public funding sources. In 2010, the Fund launched a direct investment program with the Florida Energy and Climate Commission, a state entity within the Executive Office of the Governor. The progress of direct investments by the fund must be included in the fund's annual report to the Governor, the President of the Senate, and the Speaker of the House of Representatives.

The Fund is organized as a private, not-for-profit corporation under ch. 617, F.S., and administered by Enterprise Florida, Inc ("EFI"). EFI selects a five-person appointment committee which selects a board of directors for the Fund. The board then selects a Fund investment manager. Currently, the Fund is managed by Florida First Partners, a joint venture between the Credit Suisse Customized Fund Investment Group ("CFIG") and Florida-based MILCOM Venture Partners ("MVP"). CFIG serves various client types including the states of Indiana and Oregon, endowments, family offices, and high net worth individuals. MVP is a venture capital firm focused on the intersection of the commercial and defense markets. MVP manages two venture capital funds: MILCOM Technologies, a seed-stage investment fund, and OnPointTechnologies, an early-stage venture capital fund.

##### **Infrastructure Funding in Florida**

For nearly six decades, Florida has been one of the fastest growing states in the nation, with population expanding from 3 million in 1950 to nearly 19 million in 2010.<sup>1</sup> Demand for energy, transportation, and communication systems expanded rapidly over the past several decades. Current projections suggest Florida may add an additional 5 million new residents by the year 2030.<sup>2</sup> Employment, tourism, gross state product, and income will expand as well, contributing to growth in demand for strategic infrastructure. In order to meet future capacity over the next 20-25 years, it is estimated that Florida will need:

- \$47.0 billion for highway and rail infrastructure;<sup>3</sup>
- \$29.9 billion for water and wastewater facilities and infrastructure;<sup>4</sup>
- \$3.5 billion for aviation facilities and infrastructure;<sup>5</sup>
- \$2.8 billion for seaport facilities and infrastructure,<sup>6</sup> and
- \$2.5 billion for storm water management.<sup>7</sup>

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<sup>1</sup> 2010 Census, Apportionment Population and Number of Representatives by State. United States Census Bureau. <http://2010.census.gov/news/press-kits/apportionment/apport.html> (last visited 03/07/2011).

<sup>2</sup> Florida Census Day Population: 1970-2030, Office of Economic and Demographic Research, August 2010. <http://edr.state.fl.us/Content/population-demographics/data/index.cfm> (last visited 03/07/2011).

<sup>3</sup> Strategic Intermodal System Unfunded Needs Plan, Florida Department of Transportation, May 2006. <http://www.dot.state.fl.us/planning/systems/mspi/sisnplan.shtm> (last visited 03/07/2011).

<sup>4</sup> Clean Watersheds Needs Survey 2008 Report to Congress, United States Environmental Protection Agency. <http://water.epa.gov/scitech/datait/databases/cwns/2008reportdata.cfm> (last visited 03/07/2011).

<sup>5</sup> Strategic Intermodal System Unfunded Needs Plan, May 2006.

<sup>6</sup> Strategic Intermodal System Unfunded Needs Plan, May 2006.

<sup>7</sup> Clean Watersheds Needs Survey 2008 Report to Congress.

Due to the large size and cost, and often monopolistic characteristics of these assets, infrastructure projects have historically been financed, built, owned and operated by state and local governments. Today, public entities solicit grants, borrow capital or issue bonds to pay for public infrastructure projects. However, projected infrastructure funding from all public sources – federal, state, and local – is not sufficient to pay for all needed improvements.

### **Contingent Tax Programs**

Contingent tax credits help to raise money for state-affiliated venture capital initiatives without immediately affecting state revenues. Contingent tax credit programs are statutory state guarantees established to incentivize venture capital investment into state target industries. Seven states, Arkansas, Iowa, Michigan, Ohio, Oklahoma, South Carolina and Utah, have adopted programs authorizing the issuance of contingent tax credits to investors in state-sponsored fund of funds. However, no state has created an infrastructure funding program similar to the one proposed in this bill.

### **Changes Made By the Bill**

#### **Florida Infrastructure Fund Partnership**

The bill creates s. 288.9627, F.S., which authorizes the Florida Opportunity Fund (“Fund”) to facilitate the creation of the Florida Infrastructure Fund Partnership (“Partnership”). The bill provides that the Partnership is organized and operated under ch. 620, F.S., as a private, for-profit, limited partnership or limited liability partnership and is not an instrumentality of the state.

The Fund is authorized to loan no more than \$750,000 to the Partnership for use in paying initial expenses incurred in the organization of the partnership and the solicitation of investment partners (or “partners”). Further, the Fund, as the general partner, is responsible for managing the business affairs of the Partnership, including, but not limited to:

- The engagement of its investment manager(s) to assist with the management of the Partnership;<sup>8</sup>
- Soliciting and negotiating the terms, contracting, and receiving of investment capital; and
- Receiving investment returns, paying investment partners and approving investments.

#### **Infrastructure Investments**

The bill authorizes the Partnership to make direct investments in Florida-based infrastructure projects that foster economic development and meet an important infrastructure need of the state. Infrastructure projects eligible for investment include systems and facilities related to water and wastewater, power, transportation, communications, and renewable energy.<sup>9</sup> Capital for such investments must be raised by the Partnership through “commitment agreements” with investment partners approved by the Fund’s board.<sup>10</sup> The bill provides for the issuance of certificates for future contingent tax credits to guarantee the return of investment capital from the Partnership to the Partnership’s investment partners.<sup>11</sup> Contingent tax credits would only be used to guarantee the principal investment to the partners, but not any profit. The bill also requires that the total principal investment payable to the Partnership and the total amount of contingent tax credits to be issued by the Department of Revenue (“Department”) may not exceed \$700 million. However, if the Partnership fails to obtain investment commitments totaling at least \$100 million by December 1, 2012, then the Partnership must cancel all agreements and return investment amounts back to the investment partners. The Partnership must make investments in infrastructure projects based on an evaluation of the following factors:

- The written business plan for the project, including all expected revenue sources;
- The likelihood of the project in attracting operating capital from investors, grants, or other lenders;

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<sup>8</sup> The Fund may only solicit investment managers that have maintained an office in Florida for at least two years.

<sup>9</sup> The bill defines “infrastructure project” to mean a capital project in the state for a facility or other infrastructure need in the state with respect to any of the following: water or wastewater systems, communication system, power system, transportation system, renewable energy system, ancillary or support system for any of these types of projects, or other strategic infrastructure located within the state.

<sup>10</sup> The bill defines “commitment agreement” to mean a contract between the partnership and an investment partner under which the partner commits to providing a specified amount of investment capital in exchange for an ownership interest in the partnership.

<sup>11</sup> The certificates are issued by the Florida Infrastructure Investment Trust, described later in this analysis.

- The management team for the proposed project;
- The project's job creation potential in this state;
- The financial resources of the entity proposing the project;
- The presence of reasonable safeguards to ensure the project provides a continuing benefit for residents of the state; and
- Other factors deemed by the partnership to be relevant to the likelihood of the success of the project.

### Limits on Investments

The Partnership may only invest in infrastructure projects:

- That fulfill an infrastructure need in the state;
- That raise equity or debt capital from other sources. The total amount invested in such infrastructure projects must be at least twice the amount invested by the Partnership; and
- Where measures or restrictions are legally in place to ensure that no infrastructure project will be fraudulently closed.

The Partnership may not invest more than 20 percent of its total funds available for investment in any single infrastructure project. The Partnership is also prohibited from investing in any infrastructure project authorized under the Florida Rail Enterprise Act.<sup>12</sup>

In addition, the bill prohibits the Partnership and the Fund from pledging the credit or taxing power of the state or any political subdivision of the state. Obligations of the Partnership and the Fund are not obligations of the state or any political subdivision of the state. Further, the bill forbids the Partnership and the Fund from making its debts payable out of any resources except those of the Partnership or the Fund.

The bill also provides that the Partnership may not accept any investment from or make any investment in any infrastructure project with a financial institution or company identified in s. 215.472, F.S., regarding terrorist nations or any scrutinized company as that term is defined in s. 215.473, F.S., relating to Iran and Sudan.

### **Florida Infrastructure Investment Trust**

The bill also creates s. 288.9628, F.S., to establish the Florida Infrastructure Investment Trust ("Trust"), a state beneficiary public trust, to be governed by an independent board of trustees ("board"). The board is comprised of the Chief Financial Officer, the Executive Director of the Office of Trade, Tourism, and Economic Development, and the Vice Chair of EFI., or their respective designees. The bill allows an administrative officer to act on behalf of the Trust under the direction of the board. The bill prohibits board members and the administrative officer from receiving compensation and having a financial interest in any investment partner.<sup>13</sup>

The bill authorizes the Trust to engage consultants and retain professional services, issue certificates, sell tax credits, expend funds and invest funds, and contract, bond or insure against loss. Additionally, the Trust and the Fund may seek reimbursements for expenses by charging a fee<sup>14</sup> for the issuance of certificates to investment partners.

The bill authorizes the Trust to issue certificates for redeemable tax credits to partners that make equity investments in the Partnership. A certificate issued to a partner guarantees the availability of tax credits equal to that partner's commitment agreement. Certificates issued by the Trust and related tax credits may not exceed a total aggregate of \$700 million of tax credits. Further, a certificate issued by the trust must have a specific calendar year maturity date designated by the trust of not less than twelve years after the date of issuance. A partner's certificate and related tax credits can be transferred to a new owner in whole or in part.

<sup>12</sup> Sections 341.8201 – 341.842. F.S.

<sup>13</sup> Members of the board of trustees and the administrative officer are entitled to reimbursement of their expenses.

<sup>14</sup> The fee may be no more than .25 percent of the aggregate investment capital committed to the Partnership.

### Notification and Election of Tax Credits

On the maturity date of the certificate, the bill provides that if a partner has a “net capital loss,”<sup>15</sup> the Partnership must provide written notification of this circumstance to the partner. The notification must include:

- An estimate of the fair market value of the Partnership's assets;
- The total capital investment of all partners;
- The total amount of distributions received by the partners; and
- The amount of the tax credit for which the partner is entitled to be issued.

Upon receipt of notice from the Partnership, the bill provides each partner a one-time election to:

- Have the tax credits issued;
- Authorize the Trust to sell the tax credits on behalf of the partner with the proceeds of the sale to be paid by the Trust to the partner; or
- Maintain the investment in the Partnership.

The bill requires the partner to provide written notification to the Partnership and the Trust of its election within 30 days after the partner's receipt of notification from the Partnership. Failing to provide a timely notice will result in the investment partner being deemed to have elected to maintain investment in the Partnership.

### Issuance of Tax Credits

In the event that a partner becomes eligible and elects to claim tax credits under the program, the bill provides that the Trust will, on behalf of the partner, apply to the Department for the issuance of tax credits. Tax credits certified by the Department may not exceed the partner's net capital loss. The bill requires the partner to agree in writing to transfer its interest in the Partnership to the Fund before receiving the tax credit.

### Sale of Tax Credits

The bill allows the Trust to sell tax credits on behalf of a partner. The bill authorizes the Trust to sell tax credits in an amount no more than the lesser of the maximum amount of tax credits available under the terms of the certificate issued to the partner or the amount necessary to repay a partner's net capital loss. Before receiving the proceeds from the Trust's sale of tax credits, the bill requires the partner to agree in writing to transfer its interest in the Partnership to the Fund.

### Application

Within 30 days following receipt of a partner's election or the Trust's sale of the tax credits, the Trust must notify the Partnership and apply to the Department for the issuance of tax credits in the name of the partner or purchaser. The application must include the following: the Partnership's certification of the amount of credits to be issued, the applicable taxpayer, and the tax against which the credits can be applied. Within 30 days of the receipt of an application, the bill requires the Department to issue tax credits to the partner or purchaser such credits in amount as designated by the trust in the application. Further, if the trust is unable to sell the partner's tax credits within 90 days, the bill provides the partner with the option to modify the election choice.

### Tax Offset

As provided in the bill, the amount of tax credits that may be claimed or applied against state taxes may not exceed \$150 million in one state fiscal year. The bill provides that tax credits issued by the Department can be used by their owner as an offset against any state taxes owed to the state under ch. 212, F.S., ch. 220, F.S., or ch. 624, F.S., i.e., sales, corporate, and premium insurance taxes, respectively. The owner must apply the credits as an offset against eligible taxes within seven years after the credits are issued. However, the owner of the tax credit may elect to claim the tax credit as a refund of taxes paid rather than applied as an offset against eligible taxes. Such election must occur within seven years of the date of issuance.

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<sup>15</sup> The bill defines “net capital loss” to mean an amount equal to the difference between the total investment capital actually advanced by the investment partner to the partnership and the amount of the aggregate actual distributions received by the investment partner.

### Securities Regulation

The bill provides that ch. 517, F.S., dealing with regulation of securities, does not apply to the certificates and credits transferred or sold pursuant to the provisions of the bill.

### Reporting Requirements

The bill requires an annual report to be issued by the Partnership concerning the Partnership's activities to the Governor, the President of the Senate, and the Speaker of the House of Representatives. The annual report, at a minimum, must include:

- An accounting of the amount of investment capital raised and disbursed by the Partnership and the progress of the Partnership, including the progress of infrastructure projects that have been provided direct investment by the Partnership.
- A description of the costs and benefits to the state resulting from the Partnership's investments, including a list of infrastructure projects and the costs and benefits of those projects to the state, the number of businesses and associated industries affected; the number, types, and average annual wage of jobs created or retained, and the impact of the program on the state's economy.
- Independently audited financial statements, including statements that show receipts and expenditures during the preceding fiscal year for the operational costs of the Partnership.

The bill requires the Department to provide the Trust with a written assurance that the certificates issued by the Trust will be honored by the Department. Further, the bill allows the Department to provide information relative to tax credits to the Partnership and the Trust.

The bill provides for an effective date of July 1, 2011.

#### B. SECTION DIRECTORY:

**Section 1:** Amends s. 288.9621, F.S., revising the short title.

**Section 2:** Amends s. 288.9622, F.S., relating to the findings and intent of the Legislature.

**Section 3:** Amends s. 288.9623, F.S., to provide certain definitions.

**Section 4:** Creates s. 288.9627, F.S., authorizing the creation of the Florida Infrastructure Fund Partnership and providing duties and limitations of the Partnership.

**Section 5:** Creates s. 288.9628, F.S., authorizing the creation of the Florida Infrastructure Investment Trust, establishing duties for the Trust, issuance of certificates, and applications for tax credits.

**Section 6:** Creates s. 213.053(dd), F.S., to provide confidentiality and information sharing by the Department of Revenue.

**Section 7:** Provides for an effective date of July 1, 2011.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

#### A. FISCAL IMPACT ON STATE GOVERNMENT:

##### 1. Revenues:

See Fiscal Comments.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

See Fiscal Comments.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The Partnership has potential for encouraging the funding of state infrastructure projects. If the Partnership invests in successful projects, the economic impact on the private sector will be positive.

D. FISCAL COMMENTS:

The Revenue Estimating Conference estimated that the bill will have a recurring negative indeterminate impact on both state and local government revenue. The bill provides contingent tax credits against sales and use, corporate income, and insurance premium taxes, ranging from \$0 to \$700 million, possibly beginning in 2023. No more than \$150 million in credits may be utilized in any one state fiscal year.

### III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to: require counties or municipalities to spend funds or take an action requiring the expenditure of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of a state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

### IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

None.