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 Committee on Commerce and Tourism

BILL: SB 518

INTRODUCER: Senator Hukill

SUBJECT: Economic Business Incentives

DATE: March 29, 2013 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Smith	Hrdlicka	CM	**Pre-meeting**
2.			AFT	
3.			AP	
4.				
5.				
6.				

I. Summary:

SB 518 expands the sales tax exemption for machinery and equipment for new or expanding businesses to all businesses by eliminating the 5 percent productivity requirement for expanding businesses to qualify for the tax exemption.

The bill removes the limitation on the maximum amount of tax refunds an individual participant of either the Qualified Defense Contractor and Spaceflight Business Tax Refund program or the Qualified Target Industry Tax Refund program may receive in all fiscal years.

The bill removes the requirement that all Innovation Incentive Program award funds must be approved by the Legislative Budget Commission (LBC) prior to release of funds. The bill specifies that only awards over $5 million must be approved by the LBC, awards between $2 million and $5 million must be placed on consultation with the LBC 10 days prior to release, and awards of $2 million or less may be approved without consulting the Legislature.

The bill substantially amends ss. 212.08, 288.1045, 288.106, and 288.1089, F.S.

II. Present Situation:

Sales Tax Exemption for Machinery and Equipment

Florida is one of 13 states plus the District of Columbia that levy some form of tax on the purchase of machinery and equipment used for manufacturing.[1] However, Florida does provide a sales tax exemption on such purchases[2] when the machinery and equipment is purchased for certain uses by new and expanding manufacturing businesses.[3]

For new businesses, the purchase must be made for:

- Exclusive use by a new business in spaceport activities;[4] and
- Use by a new business that manufacturers, processes, compounds, or produces for sale items of tangible personal property at fixed locations.

The new business must prove to the Department of Revenue (DOR) that the items are going to be used in a new business. The purchases have to be made before the date the business begins productive operations and delivery of the tax-exempt items must be made within 12 months of that date.

For expanding businesses, the purchase must be made for:

- Exclusive use by an expanding facility engaged in spaceport activities; or
- Use in an expanding manufacturing facility or plant unit which manufacturers, processes, compounds, or produces for sale items of tangible personal property at fixed locations in Florida.

The expanding business must prove to DOR that the items will be used to increase the productive output of the expanded facility or business by 5 percent or more. Productive output is measured for a 12-month period selected by the business after installing the machinery or equipment (within 2 years of the installation) that is compared to the output level for the 12-months immediately preceding the installation of the items.[5]

Businesses must apply to DOR for a temporary tax permit, which must be returned to DOR after all the machinery and equipment is purchased. If a qualifying business fails to apply for the permit or if DOR incorrectly determines that the business was not qualified for the permit, a business can still receive the exemption through a tax refund. DOR may conduct an audit to ensure that the purchases were made pursuant to the requirements for the exemption. If DOR finds that the purchases did not meet the requirements for the exemption, the amount of taxes exempted at the time of purchase become immediately due, plus penalties and interest.

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[1] The 13 others are: AL, AR, CA, DC, HI, KY, MN, MS, NV, NM, NC, ND, and SD. Source: National Conference of State Legislatures, *Multistate Quick Answer Charts: Sales and Use Taxes*, (on file with the Senate Commerce and Tourism Committee).

[2] Exempt purchases are limited to tangible personal property that has a depreciable life of 3 or more years. See s. 212.08(5)(b)6.a., F.S.

[3] Section 212.08(5)(b), F.S. This exemption does apply to phosphate or other solid minerals severance, mining, or processing operations.

[4] The term "spaceport activities" is defined in s. 212.02(22), F.S.

[5] Section 212.08(5)(b)6.b., F.S.

In addition to the exemption for new and expanding manufacturing businesses, industrial machinery and equipment purchased by an expanding business that manufactures tangible personal property pursuant to federal procurement regulations at fixed locations is also exempt, provided the items are used to increase productive output by 10 percent or more. Production must begin no later than 2 years following the installation of the industrial machinery and equipment.[6] This exemption operates as a refund of previously paid taxes.

The exemptions do not apply to machinery or equipment purchased or used by electric utility companies, communications companies, oil or gas exploration or production operations, publishing firms that do not export at least 50 percent of their finished product out of the state, or any firm subject to regulation by the Division of Hotels and Restaurants of the Department of Business and Professional Regulation.

Further, business property purchased for use by a business located in an enterprise zone is exempt from sales and use tax. The exemption inures to the business in the form of a refund of taxes previously paid.[7]

Qualified Defense and Space Contractor Tax Refund Program

The Qualified Defense Contractor and Space Flight Business Tax Refund (QDSC) program concept was created in 1993 by Executive Order No. 93-118, signed by Governor Chiles on August 13, 1993. The order was intended to be a response to the state's concerns that reductions in federal defense spending could result in losses to high-wage, high-technology jobs in Florida. The Legislature codified the QDSC program in law in 1996,[8] originally designating the program as the Qualified Defense Contractor Tax Refund program. The program has been amended several times in the intervening years. In 2008, the program was amended to include space flight businesses as eligible participants in the program and the program was renamed to reflect the inclusion of space flight businesses. The program is set to expire on June 30, 2014. [9, 10]

The QDSC program targets the following types of projects:

- New or consolidated Department of Defense (DOD) contracts;
- Conversion of DOD production jobs to non-defense production jobs;
- Projects involving the reuse of defense-related facilities for specific activities; or
- Contracts for the manufacturing, processing, and assembly of space flight products; and other activities related to space flight.

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[6] Section 212.08(5)(d), F.S. This exemption is limited to federal contracts with the U.S. Department of Defense, the Armed Forces, the National Aeronautics and Space Administration, and other federal agencies for which the contracts are classified for national security reasons.

[7] Section 212.08(5)(h), F.S. "Business property" does not include industrial machinery and equipment eligible for the exemption for new and expanding businesses.

[8] Ch. 96-348, L.O.F.

[9] Ch. 2008-89, L.O.F.

[10] Section 288.1045, F.S.

Depending on the type of projects, applicants must show that the project increases or creates jobs, the jobs pay a certain average annual wage, and other related information. Applicants must also receive a 20 percent match from the local government for any award unless exempt.

The QDSC program's incentive is a tax refund of $3,000 per job created or retained, or $6,000 per job if the business's project is located within a rural county or an enterprise zone. An additional $1,000 refund payment for each job created or retained is allowed if the business pays an average wage of 150 percent of the average private sector wage in the area, or an additional $2,000 per-job bonus if the business pays an average wage equal to at least 200 percent of the average private sector wage in the area.

If a business does not meet its job creation objectives, it may still receive a prorated share of the refund minus a 5 percent penalty if it creates at least 80 percent of the jobs, pays at least 90 percent of the wages, and meets all other requirements of its performance agreement.

A business may not receive refunds of more than 25 percent of the total tax refunds provided in the tax refund agreement in any fiscal year, and no more than $2.5 million in tax refunds in any fiscal year. Additionally, a business may not receive more than $7 million in tax refunds under the program. If a business reaches the cap, it does not qualify for additional projects or refund payments under the program.

A qualified defense contract or spaceflight business may claim refunds from one or more of the following taxes paid:
- Corporate income taxes;
- Sales and use taxes;
- Intangible personal property taxes;
- Excise taxes paid on documents;
- Ad valorem taxes;
- Corporate income taxes; and
- Certain state communication services taxes.

Since the QDSC program's inception, 33 QDSC applications have been approved, 15 contracts have been executed, and 5 projects have been completed, meaning that the business has met the terms of its contract and received all eligible incentive payments. Of those 15 executed contracts, 6 remain active, meaning they are eligible to receive tax refunds through the QDSC program. These 6 projects have committed to create 418 cumulative jobs. The 5 completed projects cumulatively created 1,521 new jobs, exceeding their initial commitment to create 795 new jobs.[11] In FY 2011-2012, $2,180,000 in QDSC incentives were awarded, of which $1,744,000 was awarded by the state.[12]

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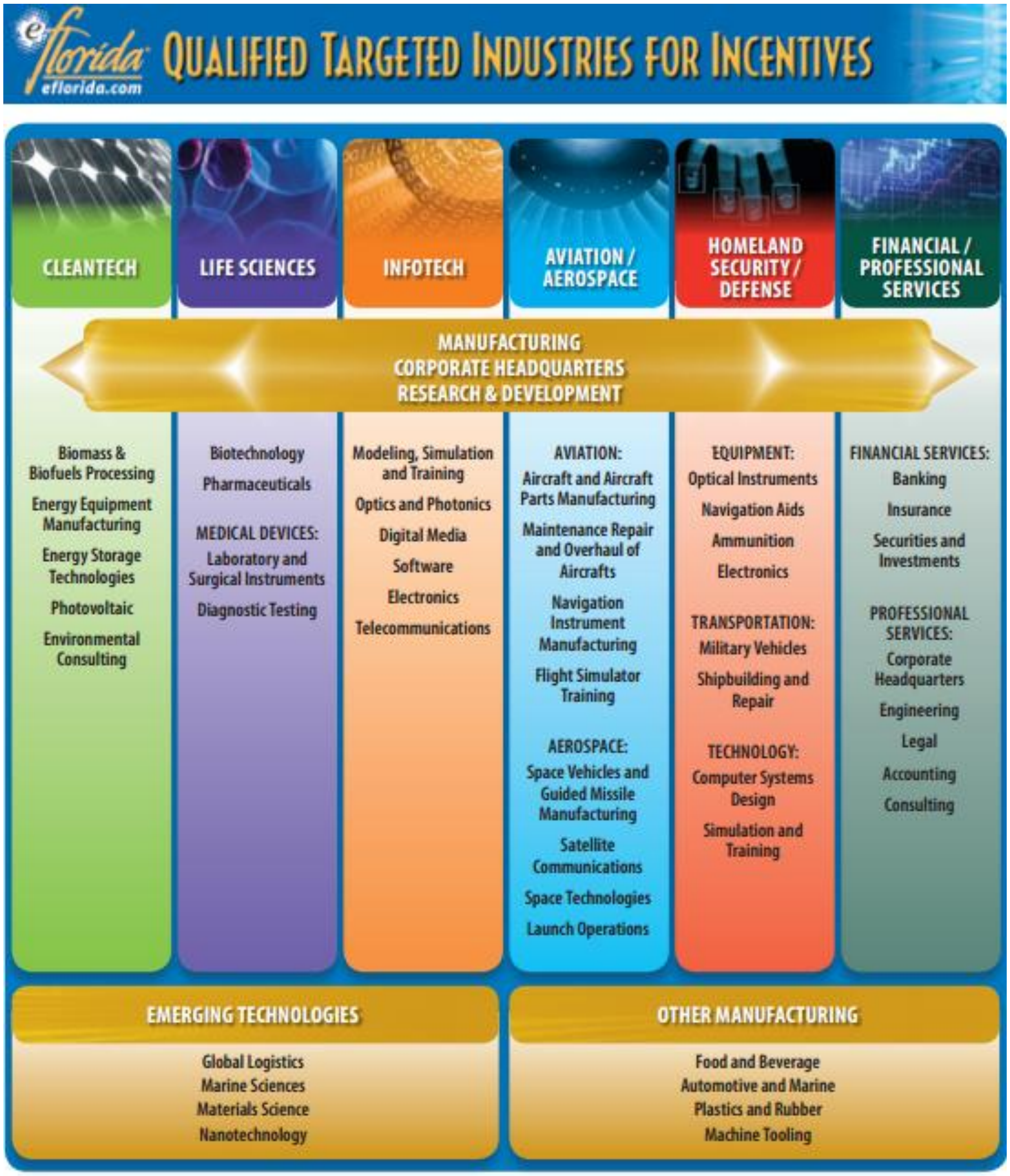
[11] An active incentive project means a business is currently performing and in good standing.
The status of each incentive falls within one of six categories: active, inactive, terminated, vacated, withdrawn, or complete.
[12] Information in this paragraph obtained from Enterprise Florida, Inc.'s, 2012 Annual Incentives Report. Available at: http://www.eflorida.com/IntelligenceCenter/download/ER/BRR_Incentives_Report.pdf, (last visited March 11, 2013).

Qualified Target Industry Tax Refund Program

The Qualified Target Industry Tax Refund (QTI) program was created by the Legislature in 1994[13] to encourage the recruitment or creation of higher-paying, higher-skilled jobs in the state by awarding eligible businesses tax refunds in exchange for creating jobs in certain target industries. The refund award level is based on wages paid, number of jobs created, and the location in the state that the business chooses to locate or expand. The QTI program is set to expire on June 30, 2020.

In order to qualify for the program, an applicant business must fall into one of Florida's target industry categories, which are developed by the Department of Economic Opportunity (DEO) and Enterprise Florida, Inc. (EFI). A diagram of targeted industries is below:[14]

[13] Ch. 94-136, L.O.F., codified as s. 288.601, F.S.
[14] The diagram is from the 2011 DEO State Job Creation Plan. Available at: http://www.eflorida.com/download/state_of_Florida_job_creation_plan.pdf, (last visited on March 11, 2013).



Applicants must show that the project increases or creates jobs, the jobs pay a certain average annual wage, and other related information. Applicants must also receive a 20 percent match from the local government for any award unless exempt.

The QTI program offers a tax refund of $3,000 per created job. The per-job tax refund increases to $6,000 if the business is located within a rural county or an enterprise zone. The program allows for tax refunds in addition to the standard awards:

- $1,000 per job if the business pays an average annual wage of at least 150 percent of the average private sector wage in the area the project is located;
- $2,000 per job if the business pays an average annual wage of at least 200 percent of the average private sector wage in the area the project is located;
- $1,000 per job if the local financial support is equal to that of the state's incentive award; and

- $2,000 per job if the business falls within one of the high-impact sectors designated under s. 288.108, F.S., or increases exports of its goods through a seaport or airport in the state by at least 10 percent in value or tonnage in each of the years that the business receives a tax refund.

A qualified target industry business may not receive more than $1.5 million in refunds in a single fiscal year, or more than $2.5 million if the project is located in an enterprise zone. Additionally, a qualified target industry business may not receive more than $7 million in refund payments in all fiscal years, or more than $7.5 million if the project is located in an enterprise zone.

A qualified target industry business may claim refunds from one or more of the following taxes paid:
- Sales and use taxes;
- Documentary stamp taxes;
- Ad valorem taxes;
- Corporate income taxes;
- Insurance premium taxes;
- Intangible personal property taxes; and
- Certain state communication taxes under ch. 202, F.S.

Since the inception of the QTI program, 1,134 QTI applications have been approved, 967 contracts have been executed, and 97 agreements have been completed. Of those 967 projects, 335 remain active, meaning they are eligible to receive tax refunds through the QTI program. These 335 projects have committed to create 45,157 jobs cumulatively. The 97 completed agreements cumulatively created 19,694 new jobs, above the initial commitment to create 19,094 new jobs. In FY 2011-2012, $58,063,500 in QTI incentives were awarded, of which $46,450,800 was awarded by the state.[15]

Innovation Incentive Program

In 2006, the Legislature created the Innovation Incentive Program for the purpose of providing resources for significant economic development projects, including high-value research and development, innovation business, and alternative and renewable energy projects.[16]

Depending on the type of project, applicants must show plans to collaborate with higher education, a 20-year break even return on the state's investment, that jobs will be created, certain capital investment amounts, availability of matching public and private funds, and other requirements.

DEO must review each application for several criteria, and must solicit comments and recommendations on the project from the Department of Agriculture and Consumer Services before making a final recommendation to the DEO Executive Director. In considering any award

[15] Information in this paragraph obtained from Enterprise Florida, Inc.'s, 2012 Annual Incentives Report. Available at: http://www.eflorida.com/IntelligenceCenter/download/ER/BRR_Incentives_Report.pdf, (last visited March 11, 2013).
[16] Chapter 2006-55, L.O.F. Codified as s. 288.1089, F.S. The scope of the program was expanded in 2008 by ch. 2008-227, L.O.F., to include "alternative and renewable energy" projects to the list of available projects.

amount, DEO must consider the amount of incentive dollars needed to cause the applicant project to locate or expand in Florida, as well as the potential for the project to stimulate additional private investment and high-quality opportunities.

Once DEO has recommended an award, the Governor must approve or deny it. The Governor is directed to consult with the President of the Senate and the Speaker of the House of Representatives prior to approving an award. DEO must include in its recommendations proposed performance conditions that an applicant project must meet in order to obtain incentive funds under the program. No funds awarded under the Innovation Incentive Program may be disbursed by the Executive Office of the Governor (EOG) until the Legislative Budget Commission (LBC) has reviewed and approved such an award.

In 2009 the Legislature required the Office of Program Policy Analysis and Government Accountability (OPPAGA) to evaluate the Innovation Incentive Program every 3 years.[17] The first report noted that despite $449 million invested in the program to bring seven major biotechnology research institutes to the state, biotechnology clusters had not yet developed in the counties where the institutes were located. The report also acknowledged that most research indicated clusters may take decades to form.[18] On March 1, 2013, OPPAGA produced its second report on the Innovation Incentive Program, finding that the state's biotechnology clusters continue to develop slowly, with the research and development sector showing the most growth between 2008 and 2011. The report also noted that the six counties where institutes are located saw varying degrees of growth in the number of cluster businesses and in employment growth, with Orange, Palm Beach, and St. Lucie counties demonstrating the largest increases in the research and development sector. The OPPAGA analysis concluded that in each of the six counties with an institute, the presence of the institute positively impacted employment growth.[19] Since the Innovation Incentive Program began in 2006, 9 applicant projects have been approved and 8 award agreements have been executed. Each of the 8 projects is still active. The 8 contracts executed required 1,771 total jobs, of which 819 jobs have been confirmed to date. In FY 2011-2012, $6,600,000 in program incentives were awarded. No awards under the Innovation Incentive Program were awarded during the 3 fiscal years prior to FY 2011-2012.[20]

III. Effect of Proposed Changes:

Section 1 amends s. 212.08(5), F.S., to expand the availability of the sales tax exemption for machinery and equipment from new or expanding businesses to all businesses. Under the bill, industrial machinery and equipment is exempt from sales tax when it is purchased for use:

- In a business that manufactures, processes, compounds, or produces for sale tangible personal property at a fixed location; or

[17] Chapter 2009-51, L.O.F.

[18] OPPAGA, *Biotechnology Clusters Developing Slowly; Startup Assistance May Encourage Growth*, (January 2010), available at: http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/1005rpt.pdf, (last visited on February 7, 2013).

[19] OPPAGA, *Florida's Biotechnology Industry is Expanding; Cluster Growth Continues to Slowly Progress*, (March 1, 2013), available at: http://www.oppaga.state.fl.us/MonitorDocs/Reports/pdf/1306rpt.pdf, (last visited on March 11, 2013).

[20] Information in this paragraph obtained from Enterprise Florida, Inc.'s, 2012 Annual Incentives Report. Available at: http://www.eflorida.com/IntelligenceCenter/download/ER/BRR_Incentives_Report.pdf, (last visited on March 11, 2013).

- In a spaceport activity, defined as an activity directed or sponsored by Space Florida on spaceport territory pursuant to its powers and responsibilities under the Space Florida Act.[21]

At the time of purchase, in order to use the exemption, the purchaser has to present a signed certificate that states that the exempt items are for exclusive use as provided above. The certificate relieves the seller of any liability to collect the tax, and if DOR later determines that tax was due, it must pursue payment from the purchaser. The exemption is available for use at any time; under current law, qualified businesses receive a temporary exemption permit.

Such expansion eliminates the 5 percent productivity requirement for expanding businesses to use the sales tax exemption. The bill eliminates the provisions to apply to DOR for a tax exemption permit. The bill also eliminates audit authority for DOR to review exempt purchases for adherence to the law. The bill eliminates rulemaking authority for DOR.

The bill makes conforming changes to the sales tax exemptions for machinery and equipment used under federal contract and for business property used in an enterprise zone.

The bill also expands the sales tax exemption for business property purchased by a business located in an enterprise zone. Under current law, if 20 percent or more of the employees are residents of an enterprise zone, the refunded sales taxes are 97 percent of taxes paid or $10,000, whichever is less. The bill reduces the residency requirement, requiring only 20 percent or less of the employees to be residents of an enterprise zone.

Section 2 amends s. 288.1045, F.S., to remove the limitation which restricts a qualified applicant from receiving more than $7 million in tax refunds in all fiscal years it participates in the Qualified Defense Contractor and Spaceflight Business Tax Refund program. This section takes effect July 1, 2013.

Section 3 amends s. 288.106, F.S., to remove the limitation which restricts a qualified target industry business from receiving more than $7 million in refund payments in all fiscal years it participates in the Qualified Target Industry Tax Refund program, or more than $7.5 million if the project is located in an enterprise zone. This section takes effect July 1, 2013.

Section 4 amends s. 288.1089, F.S., to change the requirement that all Innovation Incentive Program award funds be approved by the LBC.

The bill requires that only those awards over $5 million require approval of the LBC in order for DEO to releases award funds. Awards of less than $5 million, but greater than $2 million, require the Governor to submit a written description and evaluation of the award to the LBC at least 10 days prior to release of funds. Should the chair or vice chair of the LBC, the President of the Senate, or the Speaker of the House of Representatives advise the EOG that the proposed release of funds exceeds EOG's delegated authority or is contrary to legislative policy or intent, the Governor must void the release of funds and direct DEO to change the action until the LBC or the Legislature addresses the issue. Awards of $2 million or less may be approved by the

[21] Section 212.02(22), F.S.

Governor and funds may be released by DEO without notifying the LBC or the Legislature. The bill directs that DEO release award funds. Current law requires the Executive Office of the Governor to release the funds.

This section takes effect July 1, 2013.

Section 5 provides an effective date of July 1, 2014, except as otherwise provided in the bill.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

Article VII, s. 18 of the Florida Constitution, excuses counties and municipalities from complying with laws requiring them to spend funds or to take an action unless certain conditions are met.

Subsection (b) of the provision prohibits the Legislature from “enacting, amending, or repealing any general law if the anticipated effect” is to reduce county or municipal aggregate revenue generating authority as it existed on February 1, 1989. The exception to this prohibition is if the Legislature passes such a law by 2/3 of the membership of each chamber.

Subsection (c) of this provision prohibits the Legislature from “enacting, amending, or repealing any general law if the anticipated effect” is to reduce the percentage of a state tax shared with counties and municipalities. The exception to this prohibition is if the Legislature passes such a law by 2/3 of the membership of each chamber.

Subsection (d) provides an exemption from this prohibition. Laws determined to have an “insignificant fiscal impact,” which means an amount not greater than the average statewide population for the applicable fiscal year times $0.10 (which is $1.9 million for FY 2012-2013[22]), are exempt.[23]

The Revenue Estimating Conference has not evaluated the effects of this bill. As such, it is indeterminate whether the bill’s effect will have a significant impact on the ability of counties and municipalities to generate and share tax revenues.

B. Public Records/Open Meetings Issues:

None.

[22] Based on the Demographic Estimating Conference’s population adopted on February 7, 2013. The post-conference packet can be found at: http://edr.state.fl.us/Content/conferences/population/FDEC-Post-Conference%20Packet-201302.pdf, (last visited on March 11, 2013).

[23] *See* Florida Senate Committee on Community Affairs, *Interim Report 2012-115: Insignificant Impact*, (September 2011), available at: http://www.flsenate.gov/PublishedContent/Session/2012/InterimReports/2012-115ca.pdf, (last visited on March 11, 2013).

C. Trust Funds Restrictions:

None

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

This bill has not been evaluated by the Revenue Estimating Conference.

DEO projects that the bill will reduce state revenues by $57.7 million in FY 2013-2014, and $115.3 million each year thereafter. DEO projects the bill will reduce local revenues by $13 million in FY 2013-2014, and $26 million each year thereafter.[24]

The bill removes the lifetime cap for the amount of tax refund payments a single qualified business may receive in the QDSC and QTI tax refund programs. However, a qualified business would still be limited to the maximum annual tax refund amount of $1.5 million or $2.5 million depending on the program and the circumstances. In addition, the annual statutory funding cap of $35 million for all economic development tax refund programs would still apply.[25] Both programs will continue to be subject to annual legislative appropriations.

B. Private Sector Impact:

Businesses and consumers would likely benefit from the expansion of the machinery and equipment sales tax exemption, and more businesses will likely qualify to receive a higher refund of sales taxes paid on business equipment used in an enterprise zone.

A business may receive an unlimited amount of QDSC or QTI tax refunds over its lifetime. However, awards for QDSC and QTI are still limited to annual award limitations and appropriations.

C. Government Sector Impact:

The expanded machinery equipment sales tax exemption expected to have minimal operational impact on the Department of Revenue and the Department of Economic Opportunity.

The removal of QDSC and QTI lifetime caps is not expected to increase the resource demands of DEO.

The bill’s changes to the Innovative Incentive Program as it relates to required LBC consultations is expected to have no impact on DEO.

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[24] Department of Economic Opportunity, *Agency Bill Analysis: SB 518*, (February 4, 2013), (on file with the Senate Commerce and Tourism Committee).
[25] Section 288.095(3)(a), F.S.

VI. Technical Deficiencies:

On line 416, the letter "o" in the word "office" should be capitalized.

VII. Related Issues:

Related to the sales tax exemption for machinery and equipment, the bill does not provide any requirements for the "signed certificate" to be used to receive the exemption. It is unclear how a certificate is obtained and who signs it. The bill also eliminates audit authority for DOR to review exempt purchases for adherence to the law. Additionally, by eliminating specified rulemaking authority for DOR, the department does not have specific authority to adopt rules to implement these provisions of the bill.

The bill also removes the requirement that industrial machinery equipment be used in Florida. It is unclear if removing this requirement will allow tax-exempt machinery and equipment purchased in Florida to be used by a business outside of Florida.

Related to the sales tax exemption for business property used in an enterprise zone, the bill changes the requirement for receiving an increased refund amount from requiring that *no less than* 20 percent of the business's employees must be residents of the enterprise zone to *up to* 20 percent of the business's employees. It is unclear how this would affect businesses that employ more than 20 percent of their employees from an enterprise zone.

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:

None.