Ohio Legislative Service Commission

Thomas Kilbane

Fiscal Note & Local Impact Statement

Bill: S.B. 209 of the 131st G.A. (LSC 131 1025-2) **Date**: December 8, 2015

Status: In House Agriculture and Rural Development **Sponsor**: Sen. Hite

Local Impact Statement Procedure Required: Yes

Contents: Establishes a nonrefundable insurance tax credit for rural business growth fund investors

State Fiscal Highlights

STATE FUND	FY 2016	FY 2017	FUTURE YEARS
General Revenue Fund			
Revenues	- 0 -	- 0 -	Potential loss of several million
Expenditures	- 0 -	- 0 -	- 0 -
Ohio Rural Jobs Fund (new)			
Revenues	Potential gain	Potential gain	Potential gain
Expenditures	Potential increase	Potential increase	Potential increase

Note: The state fiscal year is July 1 through June 30. For example, FY 2016 is July 1, 2015 – June 30, 2016.

- The bill authorizes tax credits against the insurance taxes. Thus, the bill has the potential to decrease insurance tax revenue. The actual revenue loss would be dependent on the amount of credit-eligible investments and credits issued by the Development Services Agency (DSA).
- The bill provides that DSA may not approve more than $45 million in tax credit certificates over the life of the program (i.e., the tax credit cap). Thus the revenue loss to the state would not exceed $45 million, and the total would be spread across at least three years, and possibly many more years than that. Tax credits cannot be claimed during the first two years of the investment, meaning the revenue loss would begin after the current biennium.
- The insurance tax receipts against which the credits are eligible to be claimed are deposited in the GRF which would bear the majority of the revenue loss. Any reduction to GRF tax receipts would reduce the amount distributed to the Local Government Fund (LGF) and Public Library Fund (PLF), which would bear the remainder of the revenue loss.
- If the rural growth investments of a rural business growth fund do not meet certain thresholds of job creation and retention, the fund must make remittances to DSA

when making any distributions or payments to investors after the fifth anniversary of the fund. The remittances will be credited to the GRF.

- Companies seeking to establish a rural business growth fund would apply to DSA for authorization, and would be required to pay a $5,000 application fee. The bill creates the Ohio Rural Jobs Fund to receive the resulting revenue. DSA will also receive an annual fee of $50,000 (split evenly by all certified growth funds), which may offset any associated administrative expenses. However, the bill does not identify what fund will be credited with the annual fee.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2016	FY 2017	FUTURE YEARS
Counties, Municipalities, Townships, and Public Libraries (LGF and PLF)			
Revenues	- 0 -	- 0 -	Potential loss
Expenditures	- 0 -	- 0 -	- 0 -

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- Under permanent law, a share of GRF tax revenues is distributed to the LGF and the PLF. The LGF receives 1.66% of GRF tax revenue and the PLF receives 1.70%.[1] Thus, any reduction to GRF tax receipts from the bill would also reduce the amount distributed to the LGF and PLF. The potential revenue loss to each local fund would not exceed $750,000 over a period of three years.

Detailed Fiscal Analysis

The bill authorizes a nonrefundable tax credit against domestic and foreign insurance premiums taxes for certain taxpayers. If the amount of the credit for a single taxpayer in a taxable year exceeds the tax due for that year, the excess is carried forward to ensuing years until fully used. The bill provides that on and after January 15, 2016, a person that has developed a business plan to invest in rural business concerns in Ohio and has successfully solicited private investors to make capital contributions in support of the plan may apply to the Development Services Agency (DSA) for certification as a rural business growth fund.[2] DSA may then award tax credits to the investor. The bill specifies that a tax credit certificate issued may not be sold or transferred, except to an affiliate of the taxpayer that is subject to the insurance taxes.

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[1] H.B. 64 temporarily increased the PLF share to 1.70% for FYs 2016-2017. In the absence of any further action by the General Assembly, the PLF share will revert to 1.66% beginning July 1, 2017.

[2] Rural business growth funds, as defined in the bill, are essentially private investment funds licensed by the U.S. Small Business Administration or the U.S. Department of Agriculture (USDA). The funds are allowed to borrow from these federal government agencies and supplement the capital raised from private investors with access to low-cost, government-guaranteed debt.

The tax credit will be equal to the insurance company's credit-eligible capital contribution, as deemed by DSA, and may be claimed up to one-third in each of years three, four, and five after the investment was made. No credit can be claimed in years one and two. The aggregate amount of tax credits approved by DSA is limited to $45 million. Assuming DSA awards the entire amount of tax credits allowable under the bill, the potential revenue loss may be up to $15 million the first taxable year credits may be claimed. The annual revenue loss in subsequent years may be higher than $15 million, depending on credit carryover and taxpayer liabilities.

Receipts from state insurance taxes are deposited into the GRF. There is a 0.75% surtax on the premiums attributable to fire insurance. Revenue from the surtax is deposited in the Fire Marshal Fund used by the Department of Commerce. LSC assumes the tax credits are not eligible to be claimed against a surtax liability, leaving the Fire Marshal Fund unaffected by this bill. Additionally, under permanent law, a portion of the GRF tax receipts is subsequently transferred to the Local Government Fund (LGF) and the Public Library Fund (PLF), with the LGF receiving 1.66% of GRF tax revenue and the PLF receiving 1.70%. Thus, the potential revenue loss to those local funds would not exceed $1.5 million over a period of three years.

A requirement for a rural business growth fund to qualify as such with the DSA is a revenue impact assessment for the applicant's rural growth investments. The assessment must be done by a nationally recognized third-party independent economic forecasting firm and demonstrate that the business plan will result in a positive economic impact on Ohio over a ten-year period that exceeds the cumulative amount of tax credits that would be issued if the application were approved.

The bill specifies certain conditions under which DSA may recapture some tax credits, including not investing 100% of its eligible investment authority in rural growth businesses within two years of the closing date or failing to maintain an eligible investment until the fifth anniversary of the closing date.

The bill also requires a rural business growth fund to make certain payments to DSA under specific conditions. As part of the application, an estimation of the number of jobs to be created or retained in the state as a result of the rural growth investments must be provided. If certain thresholds of job growth are not met by the fifth anniversary of the fund, the rural business growth fund must make remittances to DSA when any distributions or payments that do not qualify as "eligible distributions" are made to investors.[3] The record of job creation and retention will be determined by annual reports filed by the rural business growth fund. If job creation and retention is determined to be between 50% and 75% of the original estimation, remittances will equal 25% of any distribution or payment made by the rural business growth fund. If

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[3] Eligible distributions are roughly defined as offsets for taxes related to the rural business growth fund; payment of interest and principal on a debt that does not result in less than 100% of the rural growth investment remaining invested; or distributions to cover costs and expenses related to the rural business growth fund. (R.C. 122.15 (D).)

job creation and retention is 50% of the estimate or less, remittances will equal 50% of any distributions or payments. Due to ambiguity in the timing of liquidation of a rural business growth fund, and what could qualify as an "eligible distribution" (thus exempt from the remittance requirement), it is unclear what amount of remittances to expect to be paid if the job thresholds are not met. Any remittances collected will be credited to the GRF and may reduce the revenue loss due to the insurance tax credits. Both potential remittances and credit recapture may decrease the revenue loss described earlier in this Fiscal Note.

Due to the strict criteria for eligible rural business growth funds laid out in the bill, LSC does not anticipate a large number of funds to apply or qualify. The bill requires that not more than 50% of the eligible investment authority and credit-eligible capital contributions approved under the program be awarded to the same rural business growth fund and its affiliates. The bill also requires a $5,000 fee due with an application and creates the Ohio Rural Jobs Fund, in which the application fee revenue will be deposited, to partially or fully offset additional administrative costs at DSA. Additionally, there is a $50,000 annual fee to be paid to DSA by the rural business growth funds which have been authorized by the Agency. The annual fee will be split evenly based on the number of certified funds in operation on January 1 of each year. It is unclear what fund the annual fee will be credited upon receipt by DSA.

Potential indirect fiscal effects

The bill requires the rural business growth fund applicant to show positive economic impacts from the projects receiving the credit-eligible capital from the fund. Such economic benefits may be additional employment positions created or retained; improvement in property, plant, and equipment; or a growth in rural business profits, among others. In theory, these developments would create additional tax revenue for the state and local governments. If that is realized, the fiscal revenue loss from the bill may be reduced or eliminated, particularly in locales that received business investment. However, it is also possible that those projected economic benefits may not occur.

Synopsis of Fiscal Effect Changes

The substitute bill added a provision requiring rural business growth funds to meet certain thresholds of job creation and retention as estimated during the application process. If the thresholds are not met by the fifth anniversary of the fund, remittances are required to be paid to DSA whenever any further distributions or payments to investors are made from the fund. Remittances would be credited to the GRF and could partially mitigate the revenue loss from the tax credits granted. In theory, this provision should provide a lower expected fiscal loss to the state and local governments from the bill; however, the amount of remittances received would be dependent on the timing of liquidation of the rural business growth fund and the number of distributions and payments that qualify as "eligible distributions" (exempt from the remittance requirement).

The substitute bill also adds a provision requiring an annual fee of $50,000 (aggregate) to be paid to DSA by all certified rural business growth funds. The fee will be split evenly based on the number of qualified funds in existence on January 1 each year, however, it is unclear what fund the fee will be credited upon receipt by DSA.

Other provisions added to the substitute bill relate to the eligibility of farming operations to receive investments from the funds, limits to the amount of investment authority that can be awarded to a single rural business growth fund, requirements for the portion of investment going to rural areas, the definition of "eligible distributions" by a rural business growth fund, and the start date for certification, among others. The fiscal effects of these provisions are determined to be negligible.

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