Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Technology & Economic Development Committee

HB 1422

Brief Description: Creating the Washington rural jobs act.

Sponsors: Representatives Blake, J. Walsh, Steele, Fey, Nealey, Tharinger, Chapman, Jinkins and Springer.

Brief Summary of Bill
• Creates a program to develop rural growth funds. • Creates a tax preference for taxpayers who make a capital contribution to a rural growth fund.

Hearing Date: 2/1/17

Staff: Kirsten Lee (786-7133).

Background:

Investment Companies.

Rural Business Investment Companies.

The United States Department of Agriculture (USDA) has a Rural Investment Program that aims to promote economic development and to provide a means to meet the equity capital investment needs of primarily smaller enterprises located in rural areas. Through the Rural Investment Program, the USDA licenses Rural Business Investment Companies (RBICs). Companies may apply for a RBIC license to become part of the Rural Investment Program if they are a newly formed for-profit entity or newly formed for-profit subsidiary, have a private fund management team with experience in community development or relevant venture capital financing, and are willing to invest in enterprises to create wealth and job opportunities in rural areas.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Small Business Investment Companies.

The United States Small Business Administration (SBA) has the Small Business Investment Company (SBIC) Program, which was established to increase access to capital for growth stage businesses. Through the SBIC Program, privately-owned and managed investment funds are licensed and regulated by the SBA. The SBA licenses three types of SBICs: Standard Debenture SBICs, Impact Investment SBICs, and Early Stage SBICs. Applicants must demonstrate certain qualifications, including a track record that contains investments analogous to the types that are proposed, and the SBA takes into consideration the qualifications of the applicant's fund management team.

<u>Business and Occupation Taxes</u>.

Washington's major business tax is the business and occupation (B&O) tax. The B&O tax is imposed on the gross receipts of business activities conducted within the state, without any deduction for the costs of doing business. The tax is imposed on the gross receipts from all business activities conducted within the state. Revenues are deposited in the State General Fund. There are several rate categories and a business may be subject to more than one B&O tax rate, depending on the types of activities conducted. Business and occupation taxes are collected by the Department of Revenue.

<u>Insurance Premium and Retaliatory Taxes</u>.

The Office of the Insurance Commissioner (OIC) regulates the business of insurance in Washington. The OIC must collect taxes against an insurer's premiums. Insurers pay a variety of fees and taxes, including the insurance premium tax and, in some case, retaliatory taxes.

Insurance Premium Tax.

The insurance premium tax is levied on net premiums collected or received by authorized insurers, except title insurers and fraternal benefit societies and in lieu of B&O tax. However, insurance companies do pay B &O tax on income derived from any other activities in which they engage. With some exceptions, authorized insurers are subject to a 2 percent insurance premium tax.

Retaliatory Taxes.

Washington imposes a higher tax rate on an insurer domiciled in another state or country if the state or country charges a higher tax rate on Washington-based insurance companies doing business in its jurisdiction. An alien insurer is domiciled in the state where it has established its principal office or agency, or in the country in which its laws are formed.

<u>Tax Preference Performance Statement and Expiration Date</u>.

All new tax preference legislation must include a tax preference performance statement. Tax preferences include deductions, exemptions, preferential tax rates, and tax credits. The performance statement must clearly specify the public policy objectives of the tax preference, and the specific metrics and data that will be used by the Joint Legislative Audit and Review Committee (JLARC) to evaluate the efficacy of the tax preference.

New tax preferences expire 10 years after the effective date of the tax preference, unless otherwise provided.

Summary of Bill:

The Rural Jobs Act is established to create and retain jobs in rural areas of Washington by inducing taxpayers to invest in rural growth funds with certain tax credits.

<u>Rural Growth Fund</u>.

Application.

Beginning November 1, 2017, the Department of Commerce (Department) must accept applications for approval of rural growth funds. A "rural growth fund" is an entity certified by the Department to make rural growth investments.

The application for a rural growth fund must include:

- total investment authority sought by the applicant under the business plan;
- a copy of the applicant's federal license as a RBIC or SBIC;
- evidence that the applicant has invested at least $100 million in nonpublic companies located in nonmetropolitan counties or county-equivalent units;
- an estimate of the number of jobs that will be created or retained in the state as a result of the applicant's rural growth investments;
- a business plan that includes a revenue impact assessment projecting state and local revenue to be generated by the applicant's proposed rural growth investments;
- a signed affidavit from each investor stating the amount of credit-eligible capital contributions each taxpayer commits to make. "Credit-eligible capital contributions" means an investment of cash by a person subject to Washington B&O taxes, insurance premium, or retaliatory taxes; and
- a non-refundable application fee of $5,000.

The Department must make a determination within 30 days of receipt of the application and may not approve more than $100 million in investment authority and not more than $60 million in credit-eligible capital contributions. The Department may only deny an application under certain circumstances, including when the Department has already approved the maximum allowable amount of investment authority and credit-eligible capital contributions and when credit-eligible capital contributions do not equal at least 60 percent of the total amount of investment authority sought under the applicant's plan. If an application is denied, the applicant may provide additional information to the Department for reconsideration with 15 days of the notice of denial.

If an application is approved, the rural growth fund must comply with certain requirements, including collecting cash investments and the credit-eligible capital contributions from each taxpayer issued a tax credit certificate, and providing proof of the investments to the Department.

Rural Growth Fund Investment.

Before a rural growth fund makes an investment, it may request from the Department an opinion on whether the proposed business it wishes to invest in is a rural business concern. A "rural business concern" is a business, at the time of the initial investment in the company by the rural growth fund, that:

- has fewer than 250 employees and not more than $10 million in net income for the preceding taxable year;
- has its principal place of business operations in one or more rural areas in the state; and
- is engaged in industries related to manufacturing, plant sciences, services, or technology or the Department determines the investment would be highly beneficial to the economic development for the state.

Tax Credit.

A nonrefundable tax credit, equal to the amount of the taxpayer's credit-eligible capital contribution, is allowed for taxpayers that made a credit-eligible capital contribution to a rural growth fund and were issued a tax credit certificate. The credit can be claimed against:

- B & O taxes;
- insurance premium taxes; and
- retaliatory taxes.

The credit may not be sold, transferred, or allocated to any other entity, other than an affiliate. If the amount of credit for a taxable year exceeds annual taxes due for the taxpayer, the excess credit may be carried over to subsequent taxable years until the credit is fully used. The taxpayer may claim up to one-third of the credit authorized for taxable years three, four, and five, excluding any carryover credit amounts.

To claim the credit, a taxpayer must submit a copy of the tax credit certificate and tax return for each year the credit is claimed.

Revocation of Tax Credits.

The Department must revoke a tax credit certificate issued under certain circumstances, including the failure of the rural growth fund to invest 100 percent of its investment authority in rural growth investments. The Department must provide notice of revocation to the rural growth fund and the rural growth fund has 90 days from the date of notice to cure any violations to avoid revocation.

Reporting Requirements.

Rural growth funds must submit a report to the Department on or before the fifth business day after the second anniversary of the closing date, and must submit annual reports on the last day of February of each year following the two-year report. The reports include information on rural growth investments, businesses receiving rural growth investments, and the number of employment positions created or retained because of rural growth investments.

A rural growth fund is eligible for exit and is no longer subject to regulations after six years. The state shares in the distribution of any excess funds from the rural growth funds. The amount is calculated according to the number of jobs created or retained because of the rural growth fund's rural growth investments.

The Department must adopt rules necessary to implement the Rural Jobs Act.

Tax Preference Performance Statement.

A tax preference performance statement provides that the goal of the Rural Jobs Act is to create jobs in rural areas. If the JLARC finds that the aggregate number of jobs created or retained matches or exceeds the aggregate number of jobs set forth in the business plans of approved rural growth funds in the six years following enactment of the tax preferences, then the Legislature intends to extend the tax preference. The JLARC may refer to available data, including annual reports from the rural growth funds submitted to the Department of Revenue for review.

The tax preference expires July 1, 2023.

Appropriation: None.

Fiscal Note: Available.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.