HOUSE BILL 89:
Omnibus Economic Development Improvements

2015-2016 General Assembly

Committee:	House Finance, if favorable, Appropriations	**Date:**	March 24, 2015
Introduced by:	Reps. Hamilton, R. Moore, Hanes	**Prepared by:**	Trina Griffin
Analysis of:	PCS to First Edition H89-CSSVx-7		Committee Counsel

SUMMARY: The Proposed Committee Substitute for House Bill 89 does the following:

- ***It appropriates $20 million to the Site Infrastructure Development Fund and increases the JDIG cap to $20 million.***
- ***It restores and/or extends the sunset on the following tax credits: Historic Rehabilitation Tax Credit (plus modifications), the film credit, the low-income housing credit, the renewable energy property credit, the ports credit, the qualified business investment credit, and the research and development credit.***
- ***It extends the sunset on the sales tax refunds for passenger air carriers, motorsports teams or sanctioning bodies, professional motorsports teams, and analytical services businesses.***
- ***It creates a new State tax credit modeled after the federal New Market Tax Credit Program and authorizes the Department of Commerce to charge a $5,000 nonrefundable application fee.***
- ***It would allow certain North Carolina businesses to raise funds by the sale of securities under certain circumstances by exempting the businesses from the registration and filing requirements of the North Carolina securities law. This Part includes authorization for the Secretary of State to charge a nonrefundable $150 filing fee for an exemption notice.***
- ***It requires the Department of Commerce to provide information relative to a prosperity zone to each unit of local government within the zone in order to educate and assist the local government for purposes of maximizing their economic potential and utilizing its assets for the recruitment of industry.***

CURRENT LAW & BILL ANALYSIS:

PART I. SITE INFRASTRUCTURE DEVELOPMENT FUNDING

CURRENT LAW: The Site Infrastructure Development Fund provides grants or forgivable loans to State agencies, nonprofit corporations, locals, or businesses for acquisition and/or improvement of land and to lease property to a business that (i) will invest at least $100,000,000 in private funds in a project and (ii) will employ at least 100 new employees at the project.[1] In addition, last year's budget appropriated $20M to the Job Catalyst Fund, contingent on the passage of HB1224. Because H1224 was not enacted, that amount is not being utilized.

[1] The fund was created and used in conjunction with other incentives to attract Merck and has since been depleted and inactive.

BILL ANALYSIS: Part I of the bill would transfer the $20M earmarked for JCF to SIDF to reactivate it for site development functions consistent with that Fund.

PART II. NEW MARKETS JOBS ACT OF 2015

CURRENT LAW: The State does not currently have a tax credit program modeled after the federal New Markets Tax Credit (NMTC).

BILL ANALYSIS: Part II of the bill would create a State-level tax credit that generally follows the federal New Markets Tax Credit (NMTC) under §45D of the Internal Revenue Code (IRC). The NMTC provides a subsidy (tax credit) to investors who commit capital for a 7-year term in the form of loans or equity investment to borrowers in low-income communities.

The State tax credit would be available for investments receiving the federal credit, acting as an incentive to attract the federally-credited investments to the State. Additionally, the State tax credit is available where the federal credit is not received.

North Carolina levies insurance premium tax upon insurers for the privilege of engaging in the business of providing insurance in this State. The bill would allow a tax credit to insurers paying the gross premium tax. To receive tax credits, the insurers must make investments in qualified community development entities.

The bill would allow a tax credit against the gross premium tax equal to 58% of the amount invested through federally-recognized development entities in small businesses. The statewide total investment that could qualify for the tax credit is $208.3 million with a maximum investment in any one business of $7 million, yielding $120.8 million in tax credits.

The tax credit equals 58% of the investment and is claimed during a 7 year credit period as follows: Year One: 0%; Year Two: 0%; Year Three: 12%; Year Four: 12%; Year Five: 12%; Year Six: 11%; Year Seven: 11%. The federal credit is 39% of the investment but is claimed at different percentages over the 7 year credit period. Investments could receive both the federal credit (39%) and State credit (58%), totaling 97% tax credit.

The $208.3 million investment pool is divided into 2 funds as follows:

- $156 million is allocated to the Rural Reserve to credit investments located in rural census tracts in a county designated as Tier 1 or Tier 2 by the NC Department of Commerce.
- $52 million is allocated to the Statewide Reserve to credit investments made anywhere within the State.

Qualifying investments must be made in a qualified active low-income community business (QALICB) that does not receive 15% or more of its annual revenue from the rental or sale of real estate and meets the following requirements:

- Definition of a QALICB under I.R.C. §45D includes any corporation, nonprofit corporation, or partnership if
  - At least 50% of the total gross income is derived from the active conduct of a qualified business within any low-income community.
  - A substantial portion of the use of the tangible property is within any low-income community.
  - A substantial portion of the services performed by employees are performed in any low-income community.

  - Less than 5% of the average of the aggregate unadjusted bases of the property is attributable to collectibles.
  - Less than 5% of the average of the aggregate unadjusted bases of the property is attributable to nonqualified financial property.
- US Small Business Administration (SBA) size eligibility standards that govern small business status under federal programs. The SBA sets size standards by NAICS codes. Depending on their NAICS code, small businesses must satisfy either the size limit or the employee limit:
  - Number of employees (50 to 1,500).
  - Revenues ($0.75 million to $550 million).

The program would be administered by the Department of Commerce. Entities applying to the Department of Commerce to participate must pay a nonrefundable application fee of $5,000 and pay a refundable performance deposit equal to the greater of.25% of the amount of the investment requested to be designated as a qualified investment or $500,000 to the Department for deposit in the New Markets performance guarantee account.

PART III. HISTORIC REHABILITATION TAX CREDIT

CURRENT LAW: Article 3D of Chapter 105, titled Historic Rehabilitation Tax Credits, provided a tax credit for rehabilitating income-producing historic structures (G.S. 105-129.35) and a tax credit for rehabilitating non-income-producing historic structures (G.S. 105-129.36). Article 3D expired for rehabilitation expenditures incurred on or after January 1, 2015. The former Historic Rehabilitation Tax Credits were very similar to the tax credits proposed in this bill. However, the former credits were not capped and had a higher credit percentage.

Article 3H of Chapter 105, titled Mill Rehabilitation Tax Credit, provided a tax credit for income-producing rehabilitated mill property (G.S. 105-129.71) and a tax credit for non-income-producing rehabilitated mill property (G.S. 105-129.72). Article 3H expired for rehabilitation projects for which an application for an eligibility certification is submitted on or after January 1, 2015. Rehabilitation projects with an eligibility certification remain eligible for the Mill Rehabilitation Tax Credit.

The Mill Rehabilitation Tax Credit could not be claimed for the same project as the former Historic Rehabilitation Tax Credit under Article 3D. The Mill Rehabilitation Tax Credit had a higher credit percentage (as high as 40%) than the former Historic Rehabilitation Tax Credit – making the Mill Rehabilitation Tax Credit more valuable assuming a project qualified.

BILL ANALYSIS: Part III of this bill would reestablish a historic rehabilitation tax credit after the sunset of the former Article 3D tax credits. The new historic rehabilitation tax credits would appear as Article 3L, titled Historic Rehabilitation Tax Credits Investment Program. The credit percentages are:

- Credit for rehabilitating income‑producing historic structure is the sum of the following but the tax credit cannot exceed $4,500,000:
  - 15% of expenses from $0 to $10 million
  - 10% of expenses from $10 million to $20 million
  - 5% of expenses from $0 to $20 million if the certified historic structure is located in a development tier 1 or 2 area

    - 5% of expenses from $0 to $20 million if the certified historic structure is located on an eligible targeted investment site (i.e., site that was used as a manufacturing facility or for purposes ancillary to manufacturing, as a warehouse for selling agricultural products, or as a public or private utility; is a certified historic structure; and has been at least 65% vacant for a period of at least 2 years)

- Credit for rehabilitating non-income-producing historic structures is 15% of the expense if the expense exceeds $10,000 but the tax credit cannot exceed $22,500.

The tax credit for income-producing property (G.S. 105-129.100) requires the project qualify for the federal historic rehabilitation tax credit under IRC §47. The federal credit only applies to income-producing property, effectively limiting the tax credit to commercial buildings or portions of buildings used for commercial purposes.

The tax credit for non-income-producing property (G.S. 105-129.101) applies where the federal credit is not allowed. The tax credit for non-income-producing property can apply to personal residences assuming the property meets the other requirements.

The tax credit is nonrefundable. The credit may be elected to apply against franchise tax, individual and corporate income taxes, or gross premiums tax. The credit for rehabilitating income-producing historic structures may be allocated by pass-through entities (e.g., partnerships and S corporations) among any of its owners in its discretion as long as an owner's adjusted basis in the pass-through entity is at least 40% of the credit allocated to that owner. Normally, federal and State rules require allocation of tax items by pass-through entities to meet certain tests to prevent owners from taking a disproportionate share of tax benefits.

The North Carolina Historical Commission, in consultation with the State Historic Preservation Officer, may adopt rules needed to administer the certification process and may adopt a schedule of fees for providing any certifications.

The Department of Revenue must include in the economic incentives report the following information itemized by taxpayer:

- Number of taxpayers that took the credits
- Amount of rehabilitation expenses with respect to which credits were taken
- Total cost to the General Fund of the credits taken
- For all taxpayers, total amount of tax credits claimed and the total amount of tax credits taken against current taxes, by type of tax, during the relevant tax year
- For all taxpayers, total amount of tax credits carried forward, by type of tax

New Article 3L sunsets for rehabilitation expenditures incurred on or after January 1, 2021.

Section 3(b) would limit any existing eligibility certification for Mill Rehabilitation Tax Credit under former Article 3H by expiring the certifications on January 1, 2023.

EFFECTIVE DATE: The tax credits would apply to rehabilitation expenditures incurred on or after January 1, 2015 and sunsets for rehabilitation expenditures incurred on or after January 1, 2021.

PART IV. FILM REIMBURSEMENT PROGRAM

BILL ANALYSIS: Part IV of the bill would reenact the film credit, which expired for expenses occurring on or after January 1, 2015, would change the term "credit" to "reimbursement", and would extend the sunset to January 1, 2020.

CURRENT LAW: North Carolina's film credit was a refundable income tax credit equal to 25% of the qualifying expenses spent by a production company in connection with a production. The amount of the credit with respect to a feature film production was capped at $20 million. In order to obtain the credit, the taxpayer had to have qualifying expenses in excess of $250,000. Qualifying expenses are the total amount spent in North Carolina for the following:

- Goods and services leased or purchased by a production company in connection with a production.
- Compensation and wages paid by a production company on which it remitted withholding payments to the Department of Revenue. An amount paid in excess of $1 million to an individual for compensation may not be included as a qualifying expense.
- Cost of production-related insurance coverage obtained on the production. Expenses for insurance and coverage purchased from a related member may not be included as a qualifying expense.
- Employee fringe contributions, including health, pension, and welfare contributions.
- Per diems, stipends, and living allowances paid for work being performed in this State.

The credit may be claimed for the taxable year in which the production activities are completed. The credit is computed based on all of the taxpayer's qualifying expense incurred with respect to the production, not just the qualifying expenses incurred during the taxable year. If the credit exceeds the amount of tax imposed for the taxable year reduced by the sum of all credits allowable, the Secretary must refund the excess to the taxpayer. A pass-through entity is considered a taxpayer for purposes of claiming this credit; therefore, it does not distribute the credit among its owners.

PART V. LOW-INCOME HOUSING TAX CREDITS

BILL ANALYSIS: Part V of the bill reenacts the low-income housing credit, which expired for developments to which federal credits were allocated on or after January 1, 2015, and extends the sunset for five more years until January 1, 2020.

CURRENT LAW: Congress enacted the federal Low Income Housing Tax Credit in 1986 to fund housing for low- and moderate-income households. Each state receives a limited amount of credit each year. The Internal Revenue Service (IRS) allocates the per capita low-income housing tax credit to state housing agencies such as the North Carolina Housing Finance Agency (HFA), which in turn allocate the credit to project developers who agree to lower project rents for low-income tenants.

In 1999, North Carolina authorized a State income tax credit modeled after the federal housing credit. Under current law, a taxpayer may elect to receive the credit in the form of either a credit against tax liability or a loan generated by transferring the credit to the HFA in return for a 0% interest 30-year balloon loan equal to the credit amount. Historically, project developers have almost always elected the loan option. Neither a tax refund generated by the credit, nor a loan received as a result of the transfer of the credit is considered taxable income by the State. Although a State tax refund is considered taxable income by the IRS if the taxpayer itemizes deductions, a private letter ruling from the IRS provides that the loan proceeds are not.

PART VI. RENEWABLE ENERGY PROPERTY

BILL ANALYSIS: Part VI of the bill extends for four more years the sunset for the credit for investing in renewable energy from January 1, 2016, to January 1, 2020.

CURRENT LAW: North Carolina allows a tax credit for investing in renewable energy property. The credit is equal to 35% of the cost of the property and may be taken against the franchise tax, income tax, or gross premiums tax. The credit is subject to certain ceilings depending on whether the property is used for a business purpose, nonbusiness purpose, or for an eco-industrial park. The credit must be taken in five equal installments. The credit applies to the following machinery and equipment or real property:

- Biomass equipment that uses renewable biomass resources for biofuel production of ethanol, methanol, and biodiesel; anaerobic biogas production of methane using agricultural and animal waste or garbage; or commercial thermal or electrical generation from renewable energy crops or wood waste materials.
- Hydroelectric generators.
- Solar energy equipment.
- Wind equipment.
- Geothermal heat pumps and geothermal equipment.

PART VII. NORTH CAROLINA PORTS CREDIT

BILL ANALYSIS: Part VII of the bill reenacts the State Ports credit as it existed before it expired for taxable years beginning on or after January 1, 2014, and extends the sunset to January 1, 2020.

CURRENT LAW: The 1992 General Assembly enacted the State ports income tax credit to encourage exporters to use the two State-owned port terminals at Wilmington and Morehead City. When the credit was enacted, 70% of North Carolina exporters and importers used ports in other states to move their cargo, even though the North Carolina ports had the capacity to accommodate the additional vessels and cargo.

The amount of credit allowed is equal to the amount of charges paid to the North Carolina Ports Authority in the taxable year that exceeds the average amount of charges paid to the Authority for the past three years. The credit is limited to 50% of the tax imposed on the taxpayer for the current year. Any excess credit may be carried forward and applied to the taxpayer's income tax liability for the next five years. The cumulative credit may not exceed $2 million dollars per taxpayer.

PART VIII. QUALIFIED BUSINESS INVESTMENTS

BILL ANALYSIS: Part VII of the bill reenacts the Qualified Business Investment credit as it existed before it expired for taxable years beginning on or after January 1, 2014, and extends the sunset to January 1, 2020.

CURRENT LAW: The purpose of the Qualified Business Investment tax credit is to stimulate early stage investments that help move new technologies from universities and other research laboratories to commercialization. The credit is allowed for an individual taxpayer who purchases the equity securities or subordinated debt of a qualified business venture or a qualified grantee business directly from that business. Qualifying small businesses include a business that engages primarily in manufacturing, processing, warehousing, wholesaling, research and development, or a service-related industry, a business that has received within the preceding three years funding from a federal agency under the Small Business Innovation Research Programs, a business that has been certified by a research university as currently performing under a licensing agreement with the institution for commercializing technology developed at the institution.

The credit is equal to 25% of the amount invested and may not exceed $50,000 per individual in a single taxable year. An individual investor may also claim the allocable share of credits obtained by "pass-through entities" of which the investor is an owner. Pass-through entities include limited partnerships, general partnerships, S corporations, and limited liability companies. The credit may not be taken in the year the investment is made. Instead, the credit is taken in the year following the calendar year in which the investment was made, but only if the taxpayer filed an application with the Secretary of Revenue. Any unused credit may be carried forward for the next five years.

The total amount of credits allowed to all taxpayers for investments made in a calendar year may not exceed $7.5 million. The Secretary of Revenue calculates the total amount of tax credits claimed from applications filed with the Secretary of Revenue. If the amount exceeds the cap, then the Secretary allows a portion of the tax credits claimed by allocating the total of $7.5 million in tax credits in proportion to the size of the credit claimed by each taxpayer. In general, a taxpayer forfeits the credit if the taxpayer transfers the securities within one year or the qualified business redeems the securities purchased by the taxpayer within five years after the investment was made.

PART IX. JOB DEVELOPMENT INVESTMENT GRANT PROGRAM

BILL ANALYSIS: Part IX of the bill would increase the maximum amount of total annual liability for JDIG grants awarded in a single calendar year to $20 million and would extend the sunset from January 1, 2016, to January 1, 2019.

CURRENT LAW: JDIG is a discretionary program of the State that provides funds to incentivize new or expanding business to create jobs in the State. The amount of the JDIG incentive to a company is equal to between 10% to 75% of the personal income tax withholdings generated by the eligible created positions.[2] If the business is in a tier 2 or 3 area, the incentive paid to the business is automatically reduced by 15% or 25%, respectively, and that portion is diverted into the Utility Account. The JDIG agreement can be for a term of up to 12 years. The amount that can be committed in JDIG grants has generally been capped at $15M per calendar year; however, the current cap is based on the 2013-15 biennium and is $22.5M, and the cap for 7/1/15 through 12/31/15 is $7.5M. Presuming a use of $1M of the allowed cap for a period and a term of 12 years, a $1M commitment would be paid each year of the 12-year term if the company met all required metrics, for a total commitment of $12M. The authority to enter new JDIG agreements is currently set to expire on January 1, 2016.

PART X. JUMP-START OUR BUSINESS START-UPS ACT

BILL ANALYSIS: Part X of the bill would allow NC companies to sell $1 million ($2 million in some cases) of unregistered securities to NC residents. The Secretary of State is authorized to charge a nonrefundable filing fee of $150 for filing a notice for unregistered securities. Specifically, the bill would create the Invest NC exemption that requires:

- **NC Issuer** – The issuer must be a North Carolina business entity formed under the laws of the State and registered with the Secretary of State.

[2] The amount of the incentive paid to a company is automatically decreased by 25% or 15% for tier 3 and tier 2 projects, respectively, with that percentage going to the Utility Account for infrastructure projects that are reasonably expected to create jobs in economically distressed counties (i.e. tier 1 and 2 counties).

- **Intrastate Offering** – The transaction must meet the federal exemption for an intrastate offering, which means that the issuer and all purchasers must be located in NC, that purchasers cannot transfer the securities for a period of time, that a certain percentage of the proceeds must be used in the State, and that the issuer cannot sell or have an economic impact outside the state.
- **$1/$2 Million Maximum Per Offering** – If the issuer has not undergone a financial audit, the maximum amount of cash raised under the exemption must not exceed $1 million minus the amount received in the 12 months before the exemption. If the issuer has undergone a financial audit, the maximum amount allowed is $2 million minus the amount received in the 12 months before the exemption. Offers and sales to controlling persons of the issuer are exempt from the funding cap. The funding cap will be adjusted for inflation every fifth year.
- **$2,000 Maximum Per Purchaser –** The issuer has not accepted more than $2,000 from a single purchaser, unless the purchaser is an accredited investor.
- **Notice to Secretary of State** – The issuer must file a notice with the Secretary of State no less than 10 days before beginning to offer securities under the exemption. The notice must include a disclosure statement with specified financial information that will be provided to investors and an escrow agreement between the issuer and a NC bank providing that funds received from investors will be held until the minimum target offering amount is reached and that investors may cancel their purchase if the target is not reached.
- **Issuer Not Investment Company** – The issuer may not be an investment company.
- **Notice of Unregistered Securities and Limitations on Resale** – The issuer must conspicuously display on the cover of the disclosure document a notice to investors that the securities being offered have not been registered under federal or State law, that the investor bears the risk of the investment, and that the securities are subject to limitations on resale.
- **Written Acknowledgement by Purchaser** – The issuer shall require each purchaser to certify in writing that the purchaser understands and acknowledges the securities are a high-risk speculative business venture; no state or federal governmental authority has reviewed the offering; the securities are illiquid; and the purchaser may be subject to tax on a share of the taxable income and losses of the company whether or not the purchaser sold or otherwise disposed of the securities.
- **Registration and Recordkeeping by Internet Web Sites** – If the offer and sale are made through an internet web site, the issuer and the website must provide certain information to the Secretary of State, including evidence that both are NC businesses and that all purchasers are NC residents.
- **Notice and Recordkeeping by Escrow Holder** – The bank holding the escrow funds shall notify the Secretary of State of the receipt of payments for securities and the identity and residence of the investors.
- **Registration Exemption for Web Site** – The web site is exempt from the requirement to register as a dealer or salesperson if the web site meets specified conditions.
- **Registration Exemption for Issuer's Employees** – The executives and management of the issuer are exempt from the requirement to register as a dealer or salesperson as long as they do not receive any remuneration or commission for offering and selling securities under the exemption.

- **Quarterly Reporting** – The issuer must provide a quarterly report to investors until no securities issued under the exemption are outstanding.
- **Disqualification** – The exemption does not apply if the issuer or someone affiliated with the issuer is subject to any disqualification under State or federal law.
- **Rules** – The Secretary of State may adopt rules to implement the exemption and protect investors.

The Secretary of State would be authorized to charge a nonrefundable filing fee of $150 for filing the exemption notice. The bill would also authorize the Secretary of State to adopt rules to implement the exemption on an expedited basis for the first year.

PART XI. ECONOMIC INCENTIVE REFUNDS

BILL ANALYSIS: Part XI of the bill extends the sunsets for each of the following sales tax refunds:

- **Passenger air carrier.** – From January 1, 2016, to January 1, 2020. Businesses whose primary business is scheduled passenger air transportation in interstate commerce are allowed a sales tax refund of sales tax paid on fuel in excess of $2.5M.
- **Motorsports team or sanctioning body and professional motorsports team.** - From January 1, 2016, to January 1, 2020. In 2005, the General Assembly enacted a refund of sales and use taxes paid on aviation fuel by a motorsports racing team or motorsports sanctioning body. In order to qualify for the refund, the fuel must have been used to travel to or from a motorsports event in this State, from this State to a motorsports event in another State, or to this State from a motorsports event in another State. For the purposes of the refund, a 'motorsports event' includes a motorsports race, a motorsports sponsor event, and motorsports testing.
- **Analytical services business.** - From January 1, 2014, to January 1, 2020. In 2007, the General Assembly enacted a refund limited to taxpayers who (i) are engaged in analytical services within the State and (ii) increase, in comparison to their 06-07 State fiscal year expenditures, the amount of sales and use tax paid by it in this State on tangible personal property consumed or transformed in analytical service activities. The amount of the refund is 50% of the increased amount of sales and use taxes.

PART XII. RESEARCH AND DEVELOPMENT

BILL ANALYSIS: Part VII of the bill extends the sunset for the Research and Development tax credit from January 1, 2016, to January 1, 2020.

CURRENT LAW: In 2004, the General Assembly enacted this credit as an alternative to the Bill Lee research and development credit, which was set to expire along with the entire Bill Lee Act on January 1, 2006. A taxpayer that has qualified North Carolina research expenses or North Carolina university research expenses is allowed a credit. The taxpayer must satisfy requirements related to employee wages, the provision of health insurance, the taxpayer's Occupational Safety and Health Act record, and the taxpayer's environmental record. A taxpayer with overdue tax debts is not prohibited from taking this credit.

The credit amount varies. For North Carolina university research expenses, the credit amount is equal to 20% of the amount the taxpayer paid to the university for the research and development. For all other qualified research expenses, the credit is equal to a percentage of the expenses. Specifically, the rate is

3.25% for small businesses[3] and for research and development conducted in a development tier one area. For other research and development expenditures, the rate ranges from 1.25% to 3.25% as the amount of those expenditures increases.

PART XIII. RURAL ASSISTANCE

BILL ANALYSIS: Part XIII of the bill requires the Department of Commerce to provide each unit of local government within a prosperity zone with information that would be relevant to the prosperity zone to assist with maximizing the local government's economic potential and coordinating recruitment of industry to increase the utilization of assets for economic development opportunities.

[3] A small business is a business whose annual receipts, combined with the annual receipts of all related persons, does not exceed $1,000,000.