

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1225-04
Bill No.: HCS for HBs 365, 804 and 805
Subject: Business and Commerce; Economic Development; Employees - Employers
Type: Original
Date: February 27, 2007

Bill Summary: This proposal establishes the Small Business and Entrepreneurial Growth Act to allow for the expansion of small businesses, allows the Missouri Technology Corporation to authorize tax credits and changes provisions relating to the Missouri Small Business Investment tax credit.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2008	FY 2009	FY 2010
General Revenue	(\$125,518 to Unknown)	(\$133,228 to Unknown)	(\$137,224 to Unknown)
Total Estimated Net Effect on General Revenue Fund*	(\$125,518 to Unknown)	(\$133,228 to Unknown)	(\$137,224 to Unknown)

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2008	FY 2009	FY 2010
Total Estimated Net Effect on Other State Funds*	\$0	\$0	\$0

* The fiscal impact could be divided between the General Revenue Fund and the County Foreign Insurance Fund (which ultimately goes to local school districts) if some of the tax credits are utilized against insurance premium taxes.

Numbers within parentheses: () indicate costs or losses.
 This fiscal note contains 8 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2008	FY 2009	FY 2010
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2008	FY 2009	FY 2010
General Revenue	3 FTE	3 FTE	3 FTE
Total Estimated Net Effect on FTE	3 FTE	3 FTE	3 FTE

- Estimated Total Net Effect on All funds expected to exceed \$100,000 savings or (cost).
- Estimated Net Effect on General Revenue Fund expected to exceed \$100,000 (cost).

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2008	FY 2009	FY 2010
Local Government*	\$0	\$0	\$0

*** The fiscal impact could be divided between the General Revenue Fund and the County Foreign Insurance Fund (which ultimately goes to local school districts) if some of the tax credits are utilized against insurance premium taxes.**

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration - Budget and Planning (BAP)** state the proposal combines three bills into one and proposes the following:

The legislation modifies the small business tax credit program first, by reducing the amount of credits an investor may receive for the first one hundred thousand dollars invested in a Missouri small business from forty percent to thirty percent, unless such investment is made in a business located in a rural and/or distressed community, whereby the credit received may be forty percent. The amount of tax credits currently available for this program is thirteen million dollars annually with at least four million for investments in distressed communities. The legislation reduces that annual cap to ten million dollars. The proposal could therefore increase general and state revenues by three million dollars, assuming the program is fully utilized. This program may stimulate other economic activity, but Budget and Planning does not have data to estimate the induced revenues. The Department of Economic Development may have such an estimate.

The proposal creates a tax credit program for investors who contribute venture capital to qualifying companies, taxpayers who contribute to a technology commercialization project, business expenditures for industrial research conducted at public research institutions or private non-for-profit institutions, and reserves credits for investors who contributed to the initial five million dollars of venture capital to any qualifying company. All credits are authorized by the Missouri Technology Corporation, may be carried over for three consecutive years, and are capped annually at ten million dollars for the program. The proposal could therefore lower general and state revenues by that amount. This program may stimulate other economic activity, but Budget and Planning does not have data to estimate the induced revenues. The Department of Economic Development may have such an estimate.

The proposal creates the Small Business and Entrepreneurial Growth Act; similar to the Missouri Quality Jobs program. The proposal allows eligible small businesses to retain withholding taxes for a period of up to two years. This proposal could lower general and state revenues by an unknown amount. Budget and Planning defers to the Department of Economic Development for an estimate of reduced revenues.

Oversight notes that the Small Business Development tax credit program limit of \$13 million is an aggregate cap, not an annual cap. According to the Department of Economic Development, this \$13 million aggregate cap has been exhausted; therefore, the new \$10 million annual cap, is all new tax credits that can reduce Missouri tax collections by \$10 million per year.

ASSUMPTION (continued)

Officials from the **Department of Revenue (DOR)** state this legislation establishes a new tax credit (Section 348.274) with carry-forward provisions. Personal Tax would require 1 Tax Processing Technician I for every 6,000 credits claimed.

Regarding Section 348.274, DOR's Taxation section anticipates the administration of this bill be much the same as the Quality Jobs Act is administered. A new form would be created, a new system for tracking purposes would be needed, and 1 Tax Processing Technician I would be required to administer this new "Act", so as not to impose on the production of the existing withholding tax requirements.

In summary, DOR assumes costs to the general revenue fund of approximately \$80,000 per year for the two additional FTE needed to administer this program.

Officials from the **Department of Economic Development (DED)** state the bill will allow DED to issue \$10 million in Small Business Development Tax Credits. The bill will allow the Missouri Technology Corporation (MTC) to issue \$10 million in Tax Credits for investment in Missouri business and research. For the Small Business & Entrepreneurial Growth part of the bill, DED would perform the administrative work to insure new jobs were created and insurance provided. This oversight would be similar to Quality Jobs. DED would require an Economic Development Incentive Specialist II (at \$41,052 annually) and associated costs. If the program grew larger than expected, any additional funding or resources needed would be requested through the normal state budget process.

DED assumes a positive but unknown economic impact from passage of this legislation. The Division of Workforce Development within DED assumes the New Jobs Training Credit program could be negatively impacted. The withholding from these small businesses that would normally have gone to fund this training would be diverted to/kept by the employer.

DED assumes the cost of this additional FTE would total roughly \$80,000 per year.

Oversight has, for fiscal note purposes only, changed the starting salaries for DOR's Tax Processing Tech Is and DED's Economic Development Incentive Specialist II to correspond to the second step above minimum for comparable positions in the state's merit system pay grid. This decision reflects a study of actual starting salaries for new state employees for a six month period and the policy of the Oversight Subcommittee of the Joint Committee on Legislative Research. Oversight has also removed the office space expense from the estimate of expenses from the Department of Revenue and the Department of Economic Development. Oversight assumes neither agency will incur lease expense for their additional FTE.

ASSUMPTION (continued)

Officials from the **Office of the Secretary of State (SOS)** assume many bills considered by the General Assembly include provisions allowing or requiring agencies to submit rules and regulations to implement the act. The Secretary of State's office is provided with core funding to handle a certain amount of normal activity resulting from each year's legislative session. The fiscal impact for this fiscal note to Secretary of State's office for Administrative Rules is less than \$2,500. The Secretary of State's office recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, we also recognize that many such bills may be passed by the General Assembly in a given year and that collectively the costs may be in excess of what our office can sustain with our core budget. Therefore, we reserve the right to request funding for the cost of supporting administrative rules requirements should the need arise based on a review of the finally approved bills signed by the governor.

Section 620.1892 does not contain an annual limit to the amount of withholding taxes that may be retained by employers, therefore, **Oversight** will assume a potential unknown loss of revenue to the General Revenue Fund yearly. Oversight will range this loss from \$0 (no companies utilize the program) to an unknown loss of revenue.

Oversight has reflected the potential fiscal impact of this proposal impacting the General Revenue Fund. The Small Business Development tax credits (new \$10 million annual limit) could be redeemed against insurance premium tax liabilities (Chapter 148), thereby impacting the County Foreign Insurance Fund and the County Foreign Stock Fund. The County Foreign Insurance Fund is later distributed to school districts through out the state. County Stock Funds are later distributed to the school district and county treasurer of the county in which the principal office of the insurer is located. It is unknown how each of these funds may be impacted by this tax credit each year.

Oversight compared the total tax credit issuances relative to the total tax credit redemptions for the previous three years in order to determine a relationship between the two. Oversight discovered that the annual redemptions ranged from 79 percent to 86 percent of the annual issuances. Depending on the program, the redeemed credits may have been issued several years prior and carried forward to the years studied.

Oversight assumes the state would realize some benefit from the proposal; however, Oversight assumes this benefit would be indirect and therefore, has not reflected it on the fiscal note.

This proposal would decrease Total State Revenues.

<u>FISCAL IMPACT - State Government</u>	FY 2008 (10 Mo.)	FY 2009	FY 2010
GENERAL REVENUE FUND			
<u>Costs - Department of Revenue</u>			
Personal Service	(\$36,132)	(\$44,660)	(\$46,000)
Fringe Benefits	(\$16,353)	(\$20,213)	(\$20,819)
Expense and Equipment	<u>(\$11,774)</u>	<u>(\$1,036)</u>	<u>(\$1,068)</u>
<u>Total Costs - DOR</u>	(\$64,259)	(\$65,909)	(\$67,887)
FTE Change - DOR	2 FTE	2 FTE	2 FTE
<u>Costs - DED</u>			
Personal Service	(\$29,623)	(\$36,614)	(\$37,712)
Fringe Benefits	(\$13,407)	(\$16,571)	(\$17,068)
Expense and Equipment	<u>(\$18,229)</u>	<u>(\$14,134)</u>	<u>(\$14,557)</u>
<u>Total Costs - DED</u>	(\$61,259)	(\$67,319)	(\$69,337)
FTE Change - DED	1 FTE	1 FTE	1 FTE
<u>Loss - Department of Revenue</u>			
Qualified investments in small businesses tax credits (Section 135.403)	\$0 to (\$10,000,000)	\$0 to (\$10,000,000)	\$0 to (\$10,000,000)
<u>Loss - Department of Revenue</u>			
Missouri Technology Corporation tax credits (Section 348.274)	\$0 to (\$10,000,000)	\$0 to (\$10,000,000)	\$0 to (\$10,000,000)
<u>Loss - Department of Revenue</u>			
Withholding tax revenue retained by companies (Section 620.1892)	\$0 to <u>(Unknown)</u>	\$0 to <u>(Unknown)</u>	\$0 to <u>(Unknown)</u>
ESTIMATED NET EFFECT TO THE GENERAL REVENUE FUND	<u>(\$125,518 TO UNKNOWN)</u>	<u>(\$133,228 TO UNKNOWN)</u>	<u>(\$137,224 TO UNKNOWN)</u>
Estimated Net FTE Change for General Revenue Fund	3 FTE	3 FTE	3 FTE

Note: This does not reflect the possibility that some of the tax credits could be utilized by insurance companies against insurance premium taxes. If this occurs, the loss in tax revenue would be split between the General Revenue Fund and the County Foreign Insurance Fund, which ultimately goes to local school districts.

<u>FISCAL IMPACT - Local Government</u>	FY 2008 (10 Mo.)	FY 2009	FY 2010
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT - Small Business

Small business that qualify for the programs could be fiscally impacted from this proposal.

FISCAL DESCRIPTION

Sections 135.400 and 135.403 changes the laws regarding the small business investment tax credit. In its main provisions, the bill:

- (1) Reduces the amount of the tax credit for a qualified investment in a small business from 40% to 30% of the investment, unless the small business is located in a distressed community, in which case the tax credit is reduced from 60% to 40%. A tax credit equal to 40% of an investment made in a small business located in a rural area is allowed. Tax credits will only be issued on investments up to \$100,000;
- (2) Removes the 50% tax credit for investment in a community bank or community development corporation;
- (3) Requires that \$10 million in tax credits be available each fiscal year for qualified investments in Missouri small businesses. Currently, the aggregate total amount of tax credits available for qualified investments in Missouri small businesses cannot exceed \$13 million with \$4 million reserved for distressed communities;
- (4) Removes the requirement that \$500,000 be available for tax credits for qualified investments in Missouri small businesses, community banks, or community development corporations from the Neighborhood Assistance Program; and
- (5) Prohibits the Department of Economic Development from issuing certificates without the approval of the Small Business Tax Credit Review Committee, which must review and determine the eligibility of all tax credit applications.

FISCAL DESCRIPTION (continued)

Sections 348.273 and 348.274 allows the Missouri Technology Corporation to authorize up to \$10 million in tax credits per fiscal year.

A taxpayer can receive a 30% tax credit for a contribution toward the first \$500,000 in venture capital contributed to a qualifying company or a 40% tax credit if the company is located in a rural area or distressed community.

The corporation can reserve tax credits for taxpayers who contribute the initial \$5 million in venture capital to the company. The tax credit is equal to 30% of the amount invested or 40% if the company is located in a rural area or distressed community.

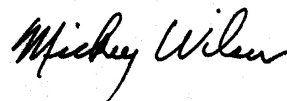
The reserved tax credits will only be issued to investors who have a net loss of investment within five years of contributing the first \$5 million in venture capital to an approved company.

Sections 620.1892 establishes the Small Business and Entrepreneurial Growth Act for small business employers who expand their business by increasing the number of jobs and meeting certain qualifications. Beginning January 1, 2008, a qualified employer can retain the Missouri withholding tax from the salaries of the newly created jobs for one year; or if the employer pays more than 50% of the cost of the premiums for health insurance for all employees, the withholding tax can be retained for two years.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Department of Economic Development
Department of Revenue
Office of Administration - Budget and Planning
Office of the Secretary of State



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Director
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