15.0700.02000

FISCAL NOTE
Requested by Legislative Council
01/22/2015

Bill/Resolution No.: SB 2328

1 A. **State fiscal effect:** *Identify the state fiscal effect and the fiscal effect on agency appropriations compared to funding levels and appropriations anticipated under current law.*

	2013-2015 Biennium		2015-2017 Biennium		2017-2019 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
Revenues						
Expenditures						
Appropriations						

1 B. **County, city, school district and township fiscal effect:** *Identify the fiscal effect on the appropriate political subdivision.*

	2013-2015 Biennium	2015-2017 Biennium	2017-2019 Biennium
Counties			
Cities			
School Districts			
Townships			

2 A. **Bill and fiscal impact summary:** *Provide a brief summary of the measure, including description of the provisions having fiscal impact (limited to 300 characters).*

SB 2328 amends the income tax law to expand the provisions governing the agricultural commodity processing facility investment tax credit.

B. **Fiscal impact sections:** *Identify and provide a brief description of the sections of the measure which have fiscal impact. Include any assumptions and comments relevant to the analysis.*

Current law requires that to qualify for the credit, an investment must be made in an agricultural commodity processing facility that is incorporated or organized in North Dakota after December 31, 2000. The bill removes this condition, opening up the use of the program to qualifying facilities incorporated or organized at any time.

Current law defines a qualifying investment as one consisting of either cash or a fee simple interest in real property located in North Dakota. The bill expands the definition to include a loan from members, shareholders, employees, suppliers, or customers of a qualifying agricultural commodity processing facility.

3. **State fiscal effect detail:** *For information shown under state fiscal effect in 1A, please:*

A. **Revenues:** *Explain the revenue amounts. Provide detail, when appropriate, for each revenue type and fund affected and any amounts included in the executive budget.*

If enacted, SB 2286 is expected to reduce state general fund revenues for the 2015-17 biennium. The amount of the reduction, if any, cannot be determined because the number of facilities utilizing the new provisions and the amount of loans are unknowns.

B. **Expenditures:** *Explain the expenditure amounts. Provide detail, when appropriate, for each agency, line item, and fund affected and the number of FTE positions affected.*

C. **Appropriations:** *Explain the appropriation amounts. Provide detail, when appropriate, for each agency and fund affected. Explain the relationship between the amounts shown for expenditures and appropriations. Indicate whether the appropriation or a part of the appropriation is included in the executive budget or relates to a continuing appropriation.*

Name: Kathryn L. Strombeck

Agency: Office of Tax Commissioner

Telephone: 328-3402

Date Prepared: 02/01/2015

2015 SENATE FINANCE AND TAXATION

SB 2328

2015 SENATE STANDING COMMITTEE MINUTES

Finance and Taxation Committee
Lewis and Clark Room, State Capitol

SB2328
2/3/2015
Job #23052

☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature Alice Grove

Explanation or reason for introduction of bill/resolution:

Relating to definition of qualified business and qualified investment under the agricultural business investment tax credit; and to provide an effective date.

Minutes: Attachment #1,

Chairman Cook opened the hearing on SB2328.

Senator Larry Luick
I am here to introduce SB2328 dealing with investment tax credits for agricultural manufacturing plants. Allen Larson is here to explain the purpose and the need for this change. I ask for favorable consideration of the bill.

Allen Larson, Business Development Manager for Minn-Dak Farmers Cooperative (Attachment #1)
In support of bill. Two primary advantages for this bill: (1) it would allow additional North Dakota manufacturers and taxpayers to benefit from this particular ag manufacturing credit; (2) it would potentially provide a net gain in the North Dakota income tax receipts.

I'd like to thank the tax department and the commerce department, as well as the North Dakota state bank. They do a wonderful job for the state of North Dakota in working with businesses that want to expand or put a new line in. They are fantastic and should receive the accolades for it.

Senator Oehlke -- Are you familiar with loans given by employees, members, share-holders now? When you get a loan that way, do you pay them an interest rate?

Allen Larson -- I'm not specifically aware of any one who has used that process. I do know that Minn-Dak has worked with a supplier in the past where we have provided them loans so that they would have the wherewithal to get the necessary equipment to become a vendor for us.

Senator Oehlke -- So you loan someone else money?

Allen Larson -- We have.

Senator Oehlke -- And you got interest rate on that?

Allen Larson -- I think we did a zero interest loan in both cases because we wanted them to be successful.

Senator Oehlke -- Is that what you would anticipate from share-holders, for instance?

Allen Larson -- That would be something that I would anticipate, yes. That or very low interest loan. I might also add that we especially designed the language of this to prevent a bank from qualifying for this because that is their ordinary course of business.

Senator Bekkedahl -- On lines 16&17 where you are adding or a loan from member share-holders, employees, suppliers or customers of a qualified business, the term in line 15 where it says qualified investment means an investment in cash, those 3 words investment in cash, do not denote that they could be a loan from members, share-holders, employees, suppliers or customers?

Allen Larson -- That's correct.

Senator Bekkedahl -- Is the added language here just for clarification, because to me the words investment in cash doesn't prohibit it from being loans from members or something like that. Can you clarify that?

Allen Larson -- I asked that exact same question of the tax department and the commerce department and the response I got was that the current legislation would not allow that. That is why we are asking for that.

Senator Triplett -- Following up on Senator Oehlke's question, you wouldn't mind if we added the phrase, or a zero interest loan, to make it clear that if they are going to be getting a tax credit they wouldn't also be entitled to interest?

Allen Larson -- I would be more than happy to have that put in there.

Chairman Cook -- Quite a list of people you have that this is available to: share-holders, employees, suppliers, customers of a qualified business.

Allen Larson -- One of the things that I thought about as we were putting this together, as an example, if you want to put a cheese plant and they need more financing for a cheese plant, this would then allow the dairies to help fund the cheese plant which would be a manufacturing plant, if it were to qualify by the commerce department. It would be a way for them to get a cheese plant started.

Chairman Cook -- We are taking about a loan that you pay back?

Allen Larson -- Right. It would need to be like a subordinated loan to the primary lender but that's to be worked out with the primary lender.

Senator Dotzenrod -- On your chart on the back page, you are going through 10 years and you are showing business activity. Do we have in state law, evidently there is a maximum or a percentage that we allow, so how did you get the $450,000?

Allen Larson -- The $450,000 is basically 10 participants who are investing $750,000 a piece. So each of those, at 30% would have a $225,000 maximum but each of those 10 participants would be limited in how much they could take in any given year. That's actually 9 of the participants would be utilizing that.

Senator Dotzenrod --Is this ag credit that is shown there, the $450,000, is that something that the entity itself, the cooperative, the ag manufacturing facility, they are not going to be preparing the returns and asking for the $450,000 credit. This is a passthrough activity that goes to the individual filer.

Allen Larson -- Yes,that is the impact of the people who invested. They are given the credits. When they go and file their own taxes, that's to reflect that.

Senator Dotzenrod -- I'm not sure if I understand, after 5 years, is that something that we have in statute? The 5 year limit?

Allen Larson -- The assumption, when I put this together, is that they would fully utilize their credits in the first 5 years.

Senator Dotzenrod -- So we have a statutory limit that applies to an individual and after 5 years each of these individuals would have maxed out what was available to them?

Allen Larson -- That's correct.

Chairman Cook -- The maximum annual credit a taxpayer may obtain under this section is $50,000 and no taxpayer may obtain more than $250,000 in credits under this section over any combination of taxable years.

Senator Dotzenrod -- And those are limits that would apply to anyone individual taxpayer which could be aggregated. You could have 10 of them or more?

Allen Larson -- Mine understanding is that each taxpayer is limited to a $250,000 lifetime.

Chairman Cook -- We have students in the room. They are nice looking and that means they are from Mandan, Christ the King. Welcome.

No further testimony.

Chairman Cook -- Matt Peyerl, do you want to answer some questions?

Matt Peyerl, Office of Tax Commissioner
A couple comments just to clarify, so that everybody is on the same page, the language in 16&17, I don't see that that would preclude a bank or financial institution, if they met one of the other categories, there is no other language in the bill to do that. Separately, the added

definition, qualified investment, is in another subsection. I think it's subsection 8 or 9 in this law that defines what a qualified investment currently is. That is equity investment. Also to Senator Dotzenrod's question about individuals and the cap, I think, it's $50,000 cap, lifetime of $250,000, but that's also available to business owners. The parent company can actually invest in a subsidiary and get $250,000 as well. It's not only individuals.

Chairman Cook -- Matt, I checked the red book this morning, I think we have 22 some tax credits available. Any of these allow a credit for loans?

Matt Peyerl -- I don't believe there are. You could view it as a fairly significant policy shift towards allowing loans for investment credit programs because investment usually comes along with ownership interests.

On line 21, as far as the effective date, I would probably offer a change as opposed to effective for a taxable year and make it effective for either projects certified after a certain date, or investments made after a certain date so there is more of a bright line if this were to pass.

Senator Oehlke -- Are there other states, that you are aware of, that do the loan thing?

Matt Peyerl -- I'm not familiar if other states have a program similar to this. One similar program that North Dakota has, is the seed capital investment tax credit which is a 45% credit for a similar type of investment

Senator Dotzenrod --On line 7, if we take an existing change out and put it back to a cooperative, that doesn't really change anything in the way this functions?

Matt Peyerl -- That was my take too. I think everyone was a little bit surprised to see that change put in. We're just fine leaving it as it was.

Senator Dotzenrod -- I'm been wondering about that date, December 31, 2000, I don't see any reason to not take it out but I'm kind of puzzled why we put it in there in the first place. Did we feel that there was going to be some investors looking back and trying to use this for things that were existing and established? And we put the date in there because we wanted it to be an incentive to be used to stimulate activity going forward rather than as a reward for something that was already established, already done?

Matt Peyerl -- I believe it's a combination of all of those things in that this is a new program starting then so it was focused on new enterprises, new activity, and as far as having some parameter around the program it has to be a new enterprise, it's almost become something that you can just create a new entity and have your new enterprise put in that entity. It's kind of an ineffective limitation if it's to serve as one anymore.

Chairman Cook closed the hearing on SB2328.

2015 SENATE STANDING COMMITTEE MINUTES

Finance and Taxation Committee
Lewis and Clark Room, State Capitol

SB2328
2/3/2015
Job #23109

☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature Alexi Grove

Explanation or reason for introduction of bill/resolution:

Minutes:

Chairman Cook opened the committee work on SB2328.

Senator Laffen -- As I understand the last part of it, if you take loaned money from someone and give them a tax credit for the loaned money, that's not something that we do anywhere right now in North Dakota. And if I'm looking to make money on my money I can't think of anywhere else I'd make better than not having to pay taxes on it, cause interest rates are like nothing right now.

Chairman Cook -- I don't believe we do that now either but I believe that if we pass this bill we will have 21 other tax credits here next session with a "me too" bill.

Senator Oehlke -- I'd move a do not pass on SB2328.

Seconded by Senator Unruh.

Senator Dotzenrod -- I' wondering if we could pass the bill with only one change and that is to take that December 31, 2000 date out of the law, rather than killing the bill. To leave the law the way it is but take that date out. Or, is that a problem too?

Chairman Cook -- That would improve it. I don't think that date means a whole lot right now anyway. I'm also wondering if we don't have another bill. We have a lot of tax credits here, if we don't have another bill that we couldn't say this tax credit is germaine to that one. Would anybody object to that? A tax credit is a tax credit.

Senator Dotzenrod -- I think that's the problem that Allan Larson had when I asked him about that date, their cooperative does not qualify because they were incorporated before this date. I think there are some problems with this idea of a loan, getting a tax credit on a loan.

Chairman Cook -- Senator Dotzenrod, taking that date out would all of a sudden make Minn-Dak Sugar available for this tax credit for contributions, not loans. That is a major policy change.

Senator Laffen -- Was it the intent of the original law to encourage new companies to start up, therefore you need a date. Or was it the intent to give everybody...

Chairman Cook -- I'd say it was to make this credit available for new. This credit, I believe, was passed in 2001. That's why there was a date.

Senator Dotzenrod -- This morning I asked that question to Matt Peyerl. Why was that date put in there originally, and the impression I got from his answer was that that date today is kind of an antique. That it doesn't really mean much. That companies can create a new name for themselves or have a subsidiary company that they form and they can use that.

Chairman Cook -- That's the answer he gave. It's ineffective. But that isn't the easiest thing for a company to do.

Senator Triplett -- Since Miss Wald is still in the room, can we ask her to answer that question?

Dee Wald -- The reason that date was put in was because they wanted to split up the seed capital and the agricultural commodity facility processing folks apart because they wanted to make sure that when you truly were a seed capital business, that's the credit you took; and that if you were an ag commodity business tax credit, we will take you out of here because of the caps, etc., that were in place at that point in time. It was important at the time. I don't know if it is now.

Any further discussion on the motion for a do not pass?

Senator Dotzenrod -- As far as the question on the date, it's not a critical thing.

Chairman Cook -- If it is, we can get a bill in next session.

Roll call vote 6-1-0.

Carrier Senator Laffen.

Date: 2-3-15

Roll Call Vote #: 1

2015 SENATE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO 2328

Senate Finance and Taxation Committee

☐ Subcommittee

Amendment LC# or Description: _____

Recommendation: ☐ Adopt Amendment
☐ Do Pass ☑ ~~Do~~ Not Pass ☐ Without Committee Recommendation
☐ As Amended ☐ Rerefer to Appropriations
☐ Place on Consent Calendar

Other Actions: ☐ Reconsider ☐ _____

Motion Made By Sen. Oehlke Seconded By Sen. Unruh

Senators	Yes	No	Senators	Yes	No
Chairman Dwight Cook	✓		Senator Jim Dotzenrod		✓
Vice Chairman Lonnie Laffen	✓		Senator Connie Triplett	✓	
Senator Brad Bekkedahl	✓				
Senator Dave Oehlke	✓				
Senator Jessica Unruh	✓				

Total (Yes) 6 No 1

Absent 0

Floor Assignment Sen. Laffen

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

SB 2328: Finance and Taxation Committee (Sen. Cook, Chairman) recommends **DO NOT PASS** (6 YEAS, 1 NAYS, 0 ABSENT AND NOT VOTING). SB 2328 was placed on the Eleventh order on the calendar.

2015 TESTIMONY

SB 2328

#1

Senate Bill 2328
Hearing Testimony February 3, 2015
North Dakota Senate Finance and Taxation Committee
Allen E Larson

Chairman Cook, Committee Members:

My name is Allen Larson, I am the Business Development Manager for Minn-Dak Farmers Cooperative, a sugar refiner owned by 500 farmers located by Wahpeton, North Dakota. I have been with Minn-Dak Farmers Cooperative for 34 years.

I was born and raised in Verona ND and have lived in North Dakota all but two years of my life.

From my perspective, passing Senate Bill 2328 would be advantageous for two reasons:

1. It would allow additional North Dakota manufacturers/farmers/taxpayers to benefit from business incentives already in the Century Code.
2. It would potentially provide for a net gain in North Dakota income tax receipts.

Attached to the back of this testimony is an example of a project and the theoretical impact it has on the local and state economy. Based on the example:

- The addition to North Dakota income tax receipts is about $3.2 million over 10-years.
- North Dakota's economy would grow by approximately $72.0 million per year.

Some background on the Ag Manufacturing Credit.

Century Code: 57-38.6-02. (3)

The director may not certify more than ten qualified businesses during each calendar year. This limitation does not apply to a qualified business that is seeking recertification during the calendar year. During the past four years, six projects or an average of 1.5 per year have been approved as qualified projects.

A link to the tax credit on the internet is:
http://www.nd.gov/tax/taxincentives/income/agcommodityitcprogram.pdf?20150202104229

Created 2001
Amended 2005, 2007, 2009, 2011

This existing law gives an income tax credit equal to 30% of the project cost up to a credit of $250,000 per qualified investor.

1.2
SB2328
2.3.15

To use any of the credit you must have North Dakota income tax liability. You may only reduce your income tax liability up to 50% of that liability and only to a maximum amount of $50,000 in any given year. You have up to ten-years (10) to use this credit.

We have worked with the Legislative Counsel, the Commerce Department and the North Dakota State Tax Department to present a modification to the Century Code that is beneficial

Therefore, we fully support the removal of the December 31, 2000 date that excludes businesses established prior to December 31, 2000 from qualifying for the credit.

For example: Under current law, if you have an agricultural manufacturing plant in your district that has been doing business since 1998 and they have a qualifying project that would add 20 jobs to your district; they would not be qualified to use this incentive to expand.

In addition, we respectfully recommend one additional change to Senate Bill 2328 in removing the change from "a" to "an existing" on line 7.

Further, we respectfully support allowing a loan for three or more years from a vested party be considered a qualified investment of cash.

At the conclusion of the three-year period, this loan would have the same impact as a preferred stock purchase, but removes or lessens some of the obstacles.

After a study by our tax firm, it was discovered that the IRS in some cases is taxing the sale of additional stock investments as ordinary income, forcing the investor to add the basis of the added stock to their permanent basis until they sell all of their interest. By allowing a loan to qualify as an investment, this IRS position may be avoided.

Most capital projects have their peak leveraging during the initial three years after start-up. During this first three-year period, the depreciation of the assets provide the working capital necessary to continue the business if it is successful.

- The loan concept would provide the necessary supplemental working capital during the initial phase of the start-up or expansion.
- If the business is successful, the business will be able to pay off the loans with permanent equity generated by the business activity.
- If the business is unsuccessful, the people who lent money to the project will likely lose their investment; therefor they are at risk and have earned their participation in this incentive.
- Whether a company buys back preferred stock or pays off the proposed loan investment, after a three year period, the company would have an identical equity balance and financial ratios.

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SB2328
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I would also like to extend my appreciation to the North Dakota Department of Commerce, the North Dakota Tax Department, the Bank of North Dakota and the other various state departments and programs that assist new opportunities become new or expanded businesses and the additional jobs that result from them.

Once again I would like to thank the committee for taking the time to address this issue. And will be happy to address any questions.

SB 2328 Ag Manufacturing Credit

	Company A	
Inside Equity	$ 17,500,000	
Traditional Loan	$ 25,000,000	
Debt from Ag Mfg	$ 7,500,000	(10 participants at $750,000 each)
Project Cost	$ 50,000,000	
Estimated Payback	5 Years	

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Total
Business Activity	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	$ 50,000,000	
Payroll	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	$ 4,000,000	
ND Goods and Services	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	$ 20,000,000	
Other Expenses	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	
Taxable Income	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	$ 10,000,000	
Business Income Tax											
Federal Incremental	34.00%	34.00%	34.00%	34.00%	34.00%	34.00%	34.00%	34.00%	34.00%	34.00%	
ND Incremental	4.53%	4.53%	4.53%	4.53%	4.53%	4.53%	4.53%	4.53%	4.53%	4.53%	
Federal Income Tax	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	$ 3,400,000	
State Income Tax	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 453,000	$ 4,530,000
Payroll Income Tax											
Federal	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%	
State	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%	2.25%	
Federal Tax	$ 600,000	$ 600,000	$ 600,000	$ 600,000	$ 600,000	$ 600,000	$ 600,000	$ 600,000	$ 600,000	$ 600,000	
State Tax	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 90,000	$ 900,000
Ag Credit Maximum	$ (450,000)	$ (450,000)	$ (450,000)	$ (450,000)	$ (450,000)						$ (2,250,000)
ND Income Tax Impact	$ 93,000	$ 93,000	$ 93,000	$ 93,000	$ 93,000	$ 543,000	$ 543,000	$ 543,000	$ 543,000	$ 543,000	$ 3,180,000
Added North Dakota business activities resulting from the transaction:											
Payroll (4x)	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	
ND Goods and Services (2x)	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	$ 40,000,000	
Other Expenses (1x)	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	$ 16,000,000	
Additional ND Activity	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	$ 72,000,000	

1.A
SB 2328
2.3.15