

2017 HOUSE FINANCE AND TAXATION

HB 1044

2017 HOUSE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Fort Totten Room, State Capitol

HB 1044
1/4/2017
26531

☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature

Mary Brucker

Explanation or reason for introduction of bill/resolution:

A bill relating to a uniform definition of a primary sector business.

Minutes:

No attachments

Chairman Headland: Opened hearing.

Vice Chairman Dockter: Introduced bill. During the interim the committee discovered several places in statute where the definition of primary sector business was a little different so the committee decided to come up with a uniform definition. This is what you have before you. Emily Thompson will describe the bill in more detail.

Chairman Headland: Are there any questions for Vice Chairman Dockter?

Emily Thompson, Counsel, Legislative Council: When the committee was looking at primary sector businesses there were nine separate instances in the century code where it was defined. The bill simply creates a definition to primary sector business in Section 1 Title 1 of the Century Code. (Emily reviewed the bill section by section and reviewed the definitions).

Chairman Headland: Could you provide the list of definitions to us?

Emily Thompson, Counsel, Legislative Council: Yes I can.

Chairman Headland: Do you think that definition is now consistent throughout the century code?

Emily Thompson, Counsel, Legislative Council: That definition is consistent because every section that previously defined primary sector business now simply states as defined in this new section of law.

Chairman Headland: Are there any questions for Emily?

Representative Steiner: What is the definition of partnership? Is it a formal partnership that is certified by Secretary of State or is a partnership a group of individuals who have come together in a foundation, for example?

Emily Thompson, Counsel, Legislative Council: I would have to sweep to see if that was defined differently in various areas of the Century Code.

Representative Schobinger: Is it common in other places in statute to require certification by a department within definition? Is this something new we're doing or is this something pretty common in definitions?

Emily Thompson, Counsel, Legislative Council: I believe I have seen that in other definitions. Off the top of my head I wouldn't be able to site exactly how many would require certification within a definition.

Chairman Headland: Any other questions for Emily? We will open it up for support for HB 1044.

Paul Lucy, Director of Economic Development and Finance Division with the Department of Commerce: We would be in support of this as it is presently structured. I would be happy to answer any questions.

Representative Ertelt: How did the Commerce Department define new wealth previously to certify it?

Paul Lucy: We define new wealth as it is presently worded in this bill right now.

Representative Olson: When the Department of Commerce goes about making the determination that a business is a primary sector business, how do you know that the products are being sold to customers outside of the state or will be sold outside the state in order to receive that determination before the business is even actually selling to customers?

Paul Lucy: Part of the application form has the company identify what their sales are; actual sales and protected sales within that to estimate or tell us the actual percentage of sales that are in state. When there is a new company that is starting up and applying for primary sector designation, which many times is necessary to do in order to access other programs, we ask them to provide us projections of their business over the next three years. Then there is a recertification process where we would relook at that business again if they wanted to continue with the certification.

Representative Olson: Is there any form of audit that goes into verifying the actual sales that are being made to out of state businesses that they claim?

Paul Lucy: There is not an audit process outside of the recertification. At that time, we would ask for the actual figures for the most recent year.

Representative Steiner: Is this part of the philosophy of the Department of Commerce for manufacturing? Do you lean more towards a physical plant that makes widgets? Is there an

exception for tourism? I know the Theodore Roosevelt Presidential Library which is starting construction in Dickinson will bring in between \$110,000 and \$250,000 new visitors internationally nationally. They are not seen by the state as really generating economic income as much as a widget that you produce and mail out. Just philosophically can you look at that draw of new people in creating wealth versus selling a widget and sending it out?

Paul Lucy: The way we presently look at it is if it is a destination tourism activity, event, or attraction. Are people coming to North Dakota specifically for that particular event, attraction, or facility? That's what our basis is for reviewing.

Representative B. Koppelman: Let's say a new business is expecting 20% of their sales to go out of state and roughly 80% will stay in state, while those similar widgets are already produced by somebody else within the state, so how would you determine whether or not they were doing enough out of state or was creating enough new wealth to meet this provision?

Paul Lucy: There is a little bit of gray area you have to deal with from time to time. Typically, it would not qualify if a company is serving primarily a local market. We also look to see if a company is operating because a resource here is in a state that they have to operate. For instance, a lot of oil service companies would meet the definition of primary sector but they are here because the oil resource is here and if the oil resource goes away the companies go away. If a business is producing a widget that is manufactured in North Dakota and there was a similar company producing a similar product in the state but there is sufficient market out there and they have a sales data at a certain level that the 20% would get to \$500,000, which was a number that was put in place before I came into the position and we've continued to follow that to a certain extent, they probably would qualify. We would look at it as if the company is competing on that national or international basis. If a company was in South Dakota or another state, would they still be competing with a company that is in North Dakota manufacturing that same widget? Would we rather have them here manufacturing or would we rather have them in Texas manufacturing? That comes into the evaluation process as well.

Representative B. Koppelman: I was on the interim committee. We put this definition in a box but it doesn't seem to make it that much clearer. Can you provide a more definitive answer as to who should fit into this box?

Paul Lucy: For the most part our guidelines include if a company has 75% of sales out of state with about \$500,000 and if they are not competing in a local market area and adding value to a product, process, or service then they would qualify. For example, a company that would sell 100% of their product produced in North Dakota we would still certify that as a primary sector. A company like Bobcat subs out manufacturing of a number of different components of their loaders. There may be a company in North Dakota that manufactures one of those components that goes into the bobcat then Bobcat takes that bobcat and sells it around the world or somewhere else in the United States, we consider that a value stream so that company would qualify. Without that component Bobcat would not complete their product and sell it outside the state and around the world or they would be finding an out of state contractor to produce it for them, it would not be in the best interest of the state to have Bobcat doing more contracting out of state as opposed to in state.

Representative Howe: Would this include research and development?

Paul Lucy: At the present time we do certify research and development as it relates to the development of a product. We wouldn't certify a research group that is a strategic think tank type of organization. I know there are some questions asking if new wealth creation definition fits well with a research and development company and we would be looking at that three-year projection but if a company is adding value to something or developing something we would see the new wealth creation as money coming in from investors and creating new wealth economic impact into the state that was not here before. If it's a local company or group doing their own research and development to develop a product and they did not do it in North Dakota, they would have to contract with someone out of state which is another part of the definition. We have administered the primary sector certification this way and will continue to do so at this time.

Representative Schobinger: This seems like this could be a really big change in definition. If you look at a company like Amazon distribution center, under the current definition it doesn't look like they would qualify as a primary sector. Under the new definition they would qualify everywhere but if the Department of Commerce didn't want to certify them as a primary sector they then wouldn't be considered. Am I reading that right?

Paul Lucy: At the present time in order for a company to access a variety of different incentive programs they have to be designated primary sector. A company like Amazon has met that definition in the past and with these changes or additions in the new wealth creation they would continue to meet that definition. I don't see this as having any real negative impact as it relates to what has qualified in the past and not being able to continue to be qualified.

Representative B. Koppelman: Your department has had a similar set of definitions that you've used. Being that it was department policy there's probably ways to meander around some of the black and white lines of that policy when you're doing in house determinations. With this being law now are you still going to be able to step in and out of the box as you see fit with your determinations like you were able to do when it was policy?

Paul Lucy: Again, I don't see this changing a whole lot. There was law in place, a definition in place, that we referred to and used to make our determination in the past. The only real change here is the addition of new wealth and the way it is worded is the way we interpreted it in the past. I don't see it having any big change or negative impact.

Chairman Headland: Further testimony in support? Is there any testimony in opposition? Seeing none we will close the hearing on HB 1044. Committee, seeing the questions that arose I believe that maybe some of us are trying to read more into what could possibly be happening here. I think it will take time for us to get our copy of the memorandum Emily wrote for the interim committee so once that is distributed to the committee members we will come back and discuss how we want to move forward with this bill. We will recess until 1:00pm.

2017 HOUSE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Fort Totten Room, State Capitol

HB 1044
1/4/2017
26553

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature

Mary Brucker

Explanation or reason for introduction of bill/resolution:

A bill relating to a uniform definition of a primary sector business.

Minutes:

Attachment 1

Chairman Headland: Are there any questions or discussion on HB 1044?

Vice Chairman Dockter: The purpose of this bill was to make sure it was consistent throughout the statute. I know you'd like to see more definite answers from the Department of Commerce when they approve primary sector but the purpose of this bill is to just make it uniform. If other people want to have more restrictions in place they would have to contact the Department of Commerce and put a separate bill in.

Chairman Headland: It's been brought to my attention that there is some concern with the definition in Subsection 4 of Section 1 where it defines primary sector. The concern is with the wording that the certification by the Department of Commerce is in the definition and by doing that you may have the possibility that someone wouldn't be certified and therefore, could never be a primary sector business.

Representative Toman: Are there other places in code with this certification in the definition? Also, what are the ramifications for including that in there? What if someone had all the qualifications minus the certification? We could keep the definition the definition but then for the purpose of providing tax incentives it must obtain certification through the Department of Commerce so they would only use the definition as the means test to see if they fit that rather than they are not that unless they are certified. It wouldn't really change it but it is just logistics. What are your thoughts on that?

Emily Thompson, Counsel, Legislative Council: Submitted definitions of primary sector business and economic development tax incentive study. Please see attachment #1. When the committee received testimony from the Department of Commerce they made a comment that was interesting and that even in some of the statutes where it already said certified by the Department of Commerce they would actually get requests to certify certain primary sector businesses in statutes that didn't have that requirement. They said on various occasions they would receive that application and certify that business as primary sector for

one of these other purposes in statute. As far as just certifying it for the tax provisions the committee can make any amendments the Chairman wishes. Just consider that if you want the definition to uniformly mean something consistently throughout the code. This is an instance where that agency reviewing some sort of application would need some type of documentation to look at those materials.

Representative Toman: Representative Schobinger, could you elaborate on some of your concerns?

Representative Schobinger: My concern is where we're placing that certification into a definition. It looks like it has been there in other places but not necessarily in all other places. This almost tells me that there's a reason in certain instances why it may have been left out or in. If we use this as a standard, then that's the standard going forward too. Is there a case where that is going to come back to get us because we made that standard throughout the code? I would feel more comfortable if the definition of a primary sector business were the definition. A definition of a primary sector business isn't necessarily a certification. I don't think in any case it's a certification. A definition is a definition. I would definitely feel more comfortable if the definition of primary sector business was what it is and the regulation or those things that come with certification come after. Section 4 of current law seems to have it right where the certification requirements come after the definition. Am I wrong about that?

Emily Thompson, Counsel, Legislative Council: You are correct. In Section 4 of the bill that is included in the definition because after the quotation mark of primary sector business it says "means" and lists all those contained in Subsection 4 so that is considered part of the definition. That section is for the low risk incentive fund and why you would see an agency doing that certification.

Representative Hatlestad: In the part with the Department of Commerce, does that give them lead way to include a business that maybe doesn't meet everything and they could certify that business to become primary sector business? Do you have to have their certification to be a primary sector business?

Chairman Headland: Yes.

Representative Hatlestad: I get the impression that you are if you are an individual corporation and so forth, or someone certified by.

Representative Schobinger: As I'm reading it a primary sector business has to be certified under the new language to be considered a primary sector.

Emily Thompson, Counsel, Legislative Council: Under the new definition it has to be certified by the Department of Commerce that is integrated into the definition that this is what it means and that is verifying the meaning. In Subsection 4 you were just discussing whether or not that qualification of being qualified as a primary sector business determined by the Department of Commerce was part of the definition, the language in Section 4 defines what primary sector business is and the last sentence in Section 4 is overstrike. The Department of Commerce is the agency that's verifying that definition. The committee discussed there was a subjective element to what is the creation of new wealth and what the percentages

and amounts are in state and out of state. Current language in Section 4 of the bill is defined and that definition includes a mandatory certification by the Department of Commerce.

Chairman Headland: The way you have it written is probably just fine. Being certified as a primary sector business doesn't mean anything. The only reason you're asking for certification is if you're applying for some type of incentive that is being authorized by the Department of Commerce. I don't see the scarecrow in here that others are probably seeing. I certainly don't have any issues with making it better if we can.

Emily Thompson, Counsel, Legislative Council: The intent of this committee when this language was crafted was when we worked with the Department of Commerce to have them individually review each of the sections you see in the bill and let the committee know if this would be kicking out certain recipients that were currently getting an incentive or qualifying under some purposes. They did not identify any concerns with applying the new language to existing law. The thought was that going forward any situations that hadn't been seen yet for different entities qualifying under a primary sector business should be contributing some kind of value or new wealth to the state. This is why new wealth was added to the definition.

Representative B. Koppelman: On line 5 number 11 where the definition begins, with what you said is in Section 4 about them being the arbiter of that do we really even need the words starting with "certified" and ending with "Economic Development and Finance"? Couldn't we just say "primary sector business means an individual, corporation, limited liability company, partnership, or association which through the employment of knowledge or labor adds value to product, process, or service which results in the creation of new wealth"? You've already said in Section 4 that they are the arbiter of that and if the arbitration yields in a certification why does it need to be in the definition? Can we just get it out of this section?

Emily Thompson, Counsel, Legislative Council: If I'm understanding your question right are you looking to pull "certify by the Department of Commerce" out and add it back in to various other sections?

Representative B. Koppelman: I thought I already understood you to say that it already exists in Section 4 where it talks about the Department of Commerce being the person who verifies this stuff. The certification itself doesn't determine whether you're a primary sector business or not, it's that you meet the criteria of employment of knowledge or labor adds value and so on. That's what we want businesses to do. A certification is just like a check mark.

Chairman Headland: I think there is some confusion on what we're trying to do on this bill. Section 4 of this bill is a different area of Century Code that is part of one particular incentive. You're asking to take the language out of that particular incentive and insert it into the definition we're going to use for all the incentives? We're trying to have a standard definition for all the incentives.

Representative B. Koppelman: Absolutely and I totally agree with the intention of our interim committee to do that. Representative Hatlestad just showed me something in Section 4 where primary sector business is on page 3 of the bill. (Read the struck out language) Maybe it's just an order of words here.

Chairman Headland: I think in order to understand that we need to have every incentive in front of us and determine exactly what each incentive is asking for. I think we're just getting deeper into this than what we should. We're trying to make a simple definition. We're complicating this.

Representative B. Koppelman: In this section if you simply made the final sentence that they do exactly what it says and certify. I'm not looking to completely change what we're doing.

Chairman Headland: If you can point out the ramifications associated with what you want to do. We have the experts telling us your questions are not really relevant. We're accomplishing things we want to accomplish with the current language. I don't know that I trust your judgement on what you believe this says over what our attorney is telling us it says. I think we're complicating things. If we're going to do this with every bill we have we're going to be here a long time. Does anyone have amendments you'd like to propose or do you want to move on this?

Representative Ertelt: In the making of definitions do we as a practice reference any other source when we're defining terms or do we simply make them up as we see fit? Does primary sector for us mean one thing and for the rest of the world mean something else? I'm looking at Black's Law Dictionary and it defines primary sector as industries that are involved in producing and extracting natural resources. We have expanded that considerably in our own law here as well as with wealth. I see this bill as adding to the definition in regard to new wealth. The definition is basically doing work to get new wealth. I think the discussion shouldn't be revolving around where the certification is but rather what new wealth is because I think that's what this bill is trying to do.

Chairman Headland: You're going to find for the purposes of bill drafts, we define certain subjects the way we want to define them. It doesn't necessarily mean it's going to follow a definition that you can pull off the internet somewhere or pertain to any other area. I can see this is going to be challenging along the way.

Representative Toman: Being on the interim committee I'm certainly behind what we were trying to do but following your previous comments that you're not trying to gain certification unless your intent is to apply for the tax credit. I kind of go back and forth on that. Why would you care about it unless you're trying to get the tax credit anyway?

Representative Olson: My opinion is that it is benign. The definition of primary sector is different in Black's Law and different here. The purpose of this bill is to uniformly identify what we're calling primary sector throughout the code and harmonize it throughout the code. Whether or not new wealth should be part of the definition of primary sector, it's already part of the definition in several sections of the code. We have new wealth throughout the code and certification by the Department of Commerce throughout the code. Whether it's right or wrong can be a debate for a different day and a different bill.

Chairman Headland: Precisely, very well put. It's a simple definition.

Representative B. Koppelman: As I understood before we didn't have a definition of new wealth prior to this bill. We had a definition of primary sector. Is that correct?

Chairman Headland: I would say that is probably wrong. I'm sure new wealth is defined in other areas of the code.

Emily Thompson, Counsel, Legislative Council: Yes, the definition of new wealth was pulled from one of the definitions of primary sector business. That was input already received from Commerce and that language was already used to define what new wealth was in another section. Currently, the only three that have black letter language in Century Code that requires certification by Commerce are for the low risk incentive fund, the sales tax exemption for primary sector businesses, computer, and telecommunication equipment, and the income tax credit for purchasing manufacturing machinery and equipment to automated manufacturing process. Other tax incentives include the tax exemptions for new and expanding business doesn't currently have language that requires Commerce to certify that business as primary sector. The certified nonprofit development corporations do not have black letter language stating that it has to be certified by Commerce nor does the c-capital investment tax credit or the income tax credit for research and experimental expenditures. If the committee wants that included for income tax incentives only you need to be aware of that. In current law there are many areas where it does apply to an incentive where it doesn't actually say it has to be certified by Commerce.

Representative Toman: For those that don't require certification I believe the Tax Department testified that they verify they qualify for those incentives, correct?

Emily Thompson, Counsel, Legislative Council: I don't know that the Tax Department does an audit for those certain tax incentives. The ones that state it must be certified by Commerce are getting their information from Commerce. If they have an issue with something normally they would look to Commerce to follow up and do that type of certification. So if it's not in statute that is some of the reason Commerce might have been certifying others that weren't specifically noted in code that had to be certified.

Representative Toman: There is no arbiter for those so we do need to set an arbiter whether it's in the definition or whether someone wants to propose an amendment that goes somewhere else. Primary sector businesses that aren't obtaining certification there's no proof saying they are doing what they say they are doing if there's no tax audit on them unless they get a tax audit. I think we should move forward with this and this formula unless someone has an amendment.

Representative Schobinger: I would probably have a proposed amendment for the Department of Commerce. On line 6 if you struck the proposed language starting with "certified by the Department of Commerce Division of Economic Development and Finance" and on line 9 after the period put back the language that's in 4, "qualifications in a primary sector business must be determined by the Department of Commerce Division of Economic Development and Finance." Would that fix anything here? All these sections jump back to that section anyway. That would keep us the same throughout the code yet separate a tiny bit a definition of primary sector business from the Department of Commerce which would

determine under a section where the primary sector business is pointed out who qualifies. The current language requires that they certify.

Chairman Headland: Does it change anything?

Emily Thompson, Counsel, Legislative Council: That language really doesn't change anything. It's just a different way to state the same thing essentially.

Chairman Headland: Does everyone understand what we're doing here? Every one of these sections is a different incentive. All we are doing is overstriking what the current language is and replacing it with number 11 all throughout the Century Code. It's as simple as that.

Representative Toman: Made a motion for a Do Pass.

Representative Hogan: Seconded.

Chairman Headland: Is there any discussion on the proposed bill?

Representative Schobinger: I'm not going to propose an amendment. I think the change here is bigger than the Chairman believes it is. We're not simply doing a definition; there are two separate thoughts and ideas. I respectfully disagree but I'm not going to propose an amendment.

Chairman Headland: Our attorney just told us that is not the case. I tend to believe our attorney when they say the language does what it says it does. In this case I'm going to reject your amendment because I believe our attorney has spoken clearly that it does. I understand you have a difference of opinion but I'm going with the bill.

Representative Schobinger: I didn't want to propose an amendment.

Chairman Headland: Is there any further discussion on the bill?

ROLL CALL VOTE: 12 YES 2 NO 0 ABSENT
MOTION CARRIES FOR DO PASS
VICE CHAIRMAN DOCKTER WILL CARRY THE BILL

Date: 1-4-17
Roll Call Vote #: 1

2017 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1044

House 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 Rep. Toman Seconded By Rep. Hogan

| Representatives | Yes | No | Representatives | Yes | No |
|---------------------------|-----|----|------------------------|-----|----|
| Chairman Headland | ✓ | | Representative Hogan | ✓ | |
| Vice Chairman Dockter | ✓ | | Representative Mitskog | ✓ | |
| Representative Ertelt | ✓ | | | | |
| Representative Grueneich | ✓ | | | | |
| Representative Hatlestad | ✓ | | | | |
| Representative Howe | ✓ | | | | |
| Representative Koppelman | | ✓ | | | |
| Representative Olson | ✓ | ✓ | | | |
| Representative Schobinger | ✓ | ✓ | | | |
| Representative Steiner | ✓ | | | | |
| Representative Toman | ✓ | | | | |
| Representative Trottier | ✓ | | | | |
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Total (Yes) 12 No 2

Absent 0

Floor Assignment Rep. Dockter

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

REPORT OF STANDING COMMITTEE

HB 1044: Finance and Taxation Committee (Rep. Headland, Chairman) recommends
DO PASS (12 YEAS, 2 NAYS, 0 ABSENT AND NOT VOTING). HB 1044 was placed
on the Eleventh order on the calendar.

2017 SENATE FINANCE AND TAXATION

HB 1044

2017 SENATE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Lewis and Clark Room, State Capitol

House Bill 1044
3/1/2017
Job #: 28536

☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 1-01-49, subsection 4 of section 10-30.5-01, subdivision b of subsection 1 of section 10-33-124, subsection 4 of section 26.1-50-01, subsection 3 of section 40-57.1-02, subsection 11 of section 52-02.1-01, subdivision b of subsection 2 of section 57-38-01.33, subdivision c of subsection 4 of section 57-38-30.5, section 57-38.5-01, and subdivision g of subsection 6 of section 57-39.2-04.3 of the North Dakota Century Code, relating to a uniform definition of a primary sector business; and to provide an effective date.

Minutes:

Attachment #1

All Senators present.

Chairman Cook: Opened the public hearing on HB 1044.

(0:00:10-0:04:25) Emily Thompson: Handed out attachment #1 and presented the information from the bill.

John Schneider, Interim Director of Economic Development and Finance, Department of Commerce: They are the agency that does the certification for the primary sector and are in support of HB 1044. The bill just makes a uniform across all of the different incentives and doesn't really change much. It is the definition for reference that has been used at commerce to certify ones in the past.

Chairman Cook: Local governments can offer property tax deductions and incentives. A few years ago, a bill was passed that limited local governments property tax incentives to primary sector businesses only, unless they put together a program that was approved by the citizens of the political subdivisions. Will this primary sector definition affect local governments?

Justin Dever, Co-Deputy Director, Department of Commerce: You are correct, legislature did approve, 2 sessions ago, for part or one of the incentives for new or expanding businesses, up to 5 years' exemption, 10 years if it's value added ag related. For that probation the companies need to be certified as primary sector for the city to grant it, unless they go through a process that would allow them to expand it to include retail. That would

have to go to a vote of the people. That provision does not apply to payment in lieu of taxes pilots, renaissance zones, tax increment financing. It only applies to new or expanding businesses.

Senator Dotzenrod: The definition on page 2, on line 6, certified by Department of Commerce. Is there a fee for that?

Justin Dever: We do not charge a fee for that certification.

Closed the hearing on HB 1044.

2017 SENATE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Lewis and Clark Room, State Capitol

House Bill 1044
3/8/2017
Job #: 28901

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact section 1-01-49, subsection 4 of section 10-30.5-01, subdivision b of subsection 1 of section 10-33-124, subsection 4 of section 26.1-50-01, subsection 3 of section 40-57.1-02, subsection 11 of section 52-02.1-01, subdivision b of subsection 2 of section 57-38-01.33, subdivision c of subsection 4 of section 57-38-30.5, section 57-38.5-01, and subdivision g of subsection 6 of section 57-39.2-04.3 of the North Dakota Century Code, relating to a uniform definition of a primary sector business; and to provide an effective date.

Minutes:

No Attachments

All Senators present.

Chairman Cook: Opened the discussion on HB 1044. Common definition of primary sector business that we heard last week. Came out of the interim committee. Went through my notes, don't see any flags. Can we kick this out?

Vice Chairman Bekkedahl moved a do pass on HB 1044.

Senator Unruh seconded.

Senator Meyer: Defined 9 times is what I had written down.

Senator Dotzenrod: If I remember, we had this in the interim and the problem is that where you went different times and places in the Century Code primary sector was defined in different ways. The idea is to have one definition and use it wherever we need it.

A Roll Call Vote was taken. 6 ayes, 0 nays, 0 absent.

Senator Cook will carry the bill.

Date: 3/6

Roll Call Vote #: 1

2017 SENATE STANDING COMMITTEE
ROLL CALL VOTES

BILL/RESOLUTION NO. 1044

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. Bekkedahl Seconded By Sen. Unruh

| Senators | Yes | No | Senators | Yes | No |
|---------------------------|-----|----|-----------------------|-----|----|
| Chairman Dwight Cook | ✓ | | Senator Jim Dotzenrod | ✓ | |
| Vice Chair Brad Bekkedahl | ✓ | | | | |
| Senator Lonnie J. Laffen | ✓ | | | | |
| Senator Jessica Unruh | ✓ | | | | |
| Senator Scott Meyer | ✓ | | | | |
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Total (Yes) 6 No 0

Absent 0

Floor Assignment Sen. Cook

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

REPORT OF STANDING COMMITTEE

HB 1044: Finance and Taxation Committee (Sen. Cook, Chairman) recommends **DO PASS** (6 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1044 was placed on the Fourteenth order on the calendar.

2017 TESTIMONY

HB 1044

STATUTORY DEFINITIONS OF PRIMARY SECTOR BUSINESS

This memorandum was requested by the interim Political Subdivision Taxation Committee to compare the various ways a primary sector business is defined throughout the North Dakota Century Code.

The phrase "primary sector business" is defined in nine separate instances throughout Century Code. The most commonly used components found in the definitions of primary sector business include components defining a primary sector business as:

1. An individual, corporation, limited liability company, partnership, or association;
2. Which through the employment of knowledge or labor adds value to a product, process, or service;
3. That results in the creation of new wealth.

A definition containing only these three components is found in Section 40-57.1-02, pertaining to tax exemptions for new and expanding businesses, which provides:

3. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association which through the employment of knowledge or labor adds value to a product, process, or service that results in the creation of new wealth.

Nearly identical definitions can be found in Sections 26.1-50-01, 57-39.2-04.3, and 57-38-01.33. These sections contain all three components, with the additional requirement that the business's status as a primary sector business be certified by the Department of Commerce. Any deviations in the language found in these three sections from the language found in Section 40-57.1-02 have been offset in bold below.

Section 26.1-50-01, pertaining to the North Dakota low-risk incentive fund, provides:

4. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association that through the employment of knowledge or labor adds value to a product, process, or service which results in the creation of new wealth. **Qualification as a primary sector business under this subsection must be determined by the department of commerce division of economic development and finance. (emphasis supplied)**

Section 57-39.2-04.3, pertaining to a sales tax exemption for primary sector business computer and telecommunications equipment, provides:

- g. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association that through the employment of knowledge or labor adds value to a product, process, or service which results in the creation of new wealth **and which has been certified by the department of commerce division of economic development and finance to be qualified under this subdivision. (emphasis supplied)**

Section 57-38-01.33, pertaining to an income tax credit for purchasing manufacturing machinery and equipment to automate a manufacturing process, provides:

- b. "Primary sector business" means **a business certified by the department of commerce** which, through the employment of knowledge or labor, adds value to a product, process, or service that results in the creation of new wealth. **(emphasis supplied)**

Definitions of a primary sector business in Sections 10-33-124 and 57-38-30.5 lack the final component of the definition provided in Section 40-57.1-02 associated with the creation of new wealth. The definition in Section 10-33-124 only pertains to adding value to a product produced for resale, rather than a product, process, or service. Any deviations in the language found in these two sections from the language found in Section 40-57.1-02 have been offset in bold below.

Section 10-33-124, pertaining to certified nonprofit development corporations, provides:

- b. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association that, through a process employing knowledge and labor, adds value to a **product produced for resale. (emphasis supplied)**

Section 57-38-30.5, pertaining to the income tax credit for research and experimental expenditures, provides:

- c. "Primary sector business" means **a qualified business** that through the employment of knowledge or labor adds value to a product, process, or service. **(emphasis supplied)**

The final three definitions of a primary sector business are found in Sections 10-30.5-01, 57-38.5-01, and 52-02.1-01 and either add or omit certain types of businesses or facilities from the definition of a primary sector business or add additional eligibility criteria. Any deviations in the language found in these three sections from the language found in Section 40-57.1-02 have been offset in bold below.

Section 10-30.5-01, pertaining to the North Dakota Development Fund, provides:

4. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association which through the employment of knowledge or labor adds value to a product, process, or service that results in the creation of new wealth. **The term includes tourism but does not include production agriculture. (emphasis supplied)**

Section 57-38.5-01, pertaining to the seed capital investment tax credit, provides:

4. "Primary sector business" means **a qualified business** that through the employment of knowledge or labor adds value to a product, process, or service and which results in the creation of new wealth **but does not include an agricultural commodity processing facility as defined under section 57-38.6-01. (emphasis supplied)**

The definition of "qualified business" in Section 57-38.5-01 requires a business to be incorporated as a corporation, passthrough entity, or joint venture.

Section 52-02.1-01, pertaining to the new jobs training program, provides:

11. "Primary sector business" means **an employer engaged in locating to or in this state which previously had no presence in this state, or in expanding its operations within this state,** which through the employment of knowledge or labor, adds value to a product, process, or **export** service that results in the creation of new wealth, **excluding production agriculture, if it meets the following eligibility criteria:**
 - a. **An employer entering into an agreement, and increasing its base employment level by at least one employee, or in the case of an employer without an established base employment level in this state creating at least five employees, within the time set in the agreement, is entitled to the new jobs credit from withholding.**
 - b. **An employer must have an economically productive and socially desirable purpose within the state.**
 - c. **An employer must not be closing or reducing its operation in one area of the state and relocating substantially the same operation in another area. (emphasis supplied)**

CONCLUSION

Though some variations exist among the nine separate definitions for a primary sector business within Century Code, many common elements are shared by them. The main differences tend to center around whether a business must be certified by the Department of Commerce; whether the addition of value to a product, process, or service must result in the creation of new wealth; and the types of entities that are included in or excluded from the definition of a primary sector business for purposes of the incentive being applied.

ECONOMIC DEVELOPMENT TAX INCENTIVE STUDY - EVALUATION CHART

The following chart was requested by the interim Political Subdivision Taxation Committee to assist the committee in tracking its progress in collecting information relative to the considerations outlined in North Dakota Century Code Section 54-35-26.

| | Agriculture Commodity Processing Facility Investment | Angel Fund Investment Tax Credit | Biodiesel Fuel Credits | Certified Nonprofit Development Corporation Investment Credit | Electrical Generating Facilities Sales Tax Exemption | Geothermal, Solar, Wind, and Biomass Energy Device Credit | Internship Program Credit | Manufacturing Automation Tax Credit | Microbusiness Income Tax Credit | New Jobs Credit From Income Tax Withholding | New or Expanding Business Income Tax Exemption | Renaissance Zone Income Tax Credits and Exemptions | Research Expense Tax Credit | Seed Capital Investment Tax Credit | Soybean or Canola Crushing Facility Credit | Telecommunications Infrastructure Sales Tax Exemption | Wage and Salary Credit | Workforce Recruitment Credit |
|--|--|----------------------------------|------------------------|--|---|--|---------------------------|--|---------------------------------|--|---|---|-----------------------------|---------------------------------------|---|--|------------------------|------------------------------|
| 1. The extent of achievement of the goals of the incentive and whether unintended consequences have developed in its application. | | X | | X | X | | | | X | | | | | X | X | X | X | |
| 2. Whether the design and application of the incentive can be improved. | | X | | X | | | | X | X | | | | | | X | X | X | |
| 3. The extent of complementary or duplicative effect of other incentives or governmental programs. | X | X | | X | | | | | X | | | | | X | X | | X | |
| 4. Whether the incentive has a positive influence on business behavior or rewards business behavior that is likely to have occurred without the incentive. | X | X | X | X | X | | | X | X | | | | | X | X | X | X | |
| 5. The effect of the incentive on the state economy, including the extent of primary sector operation of the recipient and any competitive disadvantage imposed or benefit conferred on other state businesses, any benefit or burden created for local government, and the extent of the incentive's benefit that flows to out-of-state concerns. | X | X | | X | X | | | | X | | X | | | X | X | X | X | |
| 6. The employment opportunities generated by the incentive and the extent those represent career opportunities. | X | X | | X | | | | X | X | | | | | X | X | | X | |
| 7. Whether the incentive is the most effective use of state resources to achieve desired goals. | X | | | X | X | | | X | X | | X | | | X | X | X | X | |
| 8. If the committee's analysis of the incentive is constrained by lack of data, whether statutory or administrative changes should be made to improve collection and availability of data. | | X | X | X | X | | | | X | | | | | | X | | X | X |

ECONOMIC DEVELOPMENT TAX INCENTIVE STUDY - WAGE AND SALARY CREDIT

Pursuant to North Dakota Century Code Section 54-35-26, created by 2015 Senate Bill No. 2057, a variety of economic development tax incentives are to be reviewed by a Legislative Management interim committee over the ensuing six-year period. The study is aimed at ensuring that economic development tax incentives are serving their intended purposes in a cost-effective and equitable manner. This memorandum has been provided to assist in the review of the wage and salary credit and provides an explanation of the incentive, the perceived goals of the Legislative Assembly in creating or altering the incentive, and the data and testimony that will be required to conduct an effective analysis of the incentive.

EXPLANATION OF THE WAGE AND SALARY CREDIT

Section 57-38-30.1 provides for corporate income tax credit for new industry, which is defined as "a corporate enterprise engaged in assembling, fabricating, manufacturing, mixing, or processing of any agricultural, mineral, or manufactured products or any combination thereof." The taxpayer must be a domestic corporation, which is not the result of a business reorganization or acquisition, incorporated in this state for the first time after January 1, 1969, or a foreign corporation that has received a certificate of authority to transact business in this state after January 1, 1969.

The amount of the credit is equal to 1 percent of wages and salaries paid by the corporate income taxpayer in each of the first three tax years of operation and in an amount equal to one-half of 1 percent of wages and salaries paid by the taxpayer during the fourth and fifth tax years of operation. A corporation receiving a property or income tax exemption pursuant to Chapter 40-57.1 as a new and expanding business is not eligible to receive the credit.

PERCEIVED GOALS OF THE LEGISLATIVE ASSEMBLY IN CREATING OR ALTERING THE WAGE AND SALARY CREDIT

Section 57-38-30.1, providing for a corporate income tax credit for new industry, was created through the passage of 1969 House Bill No. 464. The bill provided for a corporate income tax credit equal to 1 percent of wages and salaries paid by the corporate income taxpayer in each of the first three tax years of operation and in an amount equal to one-half of 1 percent of wages and salaries paid by the taxpayer during the fourth and fifth tax years of operation. Upon a review of the legislative history pertaining to House Bill No. 464, the perceived goal of the Legislative Assembly in creating this credit was to provide an incentive to encourage new industry to locate to this state. The estimated fiscal effect of the corporate income tax credit for new industry could not be determined during the 1969 legislative session.

Any additional changes made to the language of Section 57-38-30.1, as originally enacted, have been essentially technical in nature. These changes were effectuated by 1971 House Bill No. 1164, 1973 House Bill No. 1440, and 1995 Senate Bill No. 2191. The credit has been used relatively infrequently since its enactment.

DATA AND TESTIMONY REQUIRED TO CONDUCT AN EFFECTIVE ANALYSIS OF THE WAGE AND SALARY CREDIT

The interim Political Subdivision Taxation Committee identified various items of data and testimony that would need to be collected to effectively analyze the wage and salary credit. The following list identifies the information the committee sought to collect and the receipt of that information throughout the course of the 2015-16 interim.

1. The number of claimants and the fiscal impact of the incentive.
 - Information (Appendix A) provided to the Political Subdivision Taxation Committee by the Tax Department on December 2, 2015, indicated the total amount of the credit claimed in tax years 2006 through 2010 cannot be disclosed due to confidentiality restrictions as the credit was claimed on less than five returns in each tax year. The credit was not claimed on any corporate income tax returns in tax years 2011 through 2014.
2. The use of similar incentives in other states.
 - Incentives similar to this state's wage and salary credit (Appendix B) were found in 13 other states.
3. Employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive.
 - The committee has not identified any employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive as the incentive has not been claimed by any taxpayers in the last several years.

4. Negative impacts created as a result of the incentive.

- The committee has not identified any negative impacts created as a result of the incentive as the incentive has not been claimed by any taxpayers in the last several years.

5. Benefits that flow to out-of-state concerns resulting from the incentive.

- The committee has not identified any negative impacts created as a result of the incentive as the incentive has not been claimed by any taxpayers in the last several years.

6. Testimony from interested parties.

- Testimony has not been received from parties in support of retaining the wage and salary credit.
- Testimony (Appendix C) was provided by the Economic Development Association of North Dakota in support of eliminating the wage and salary credit.

ATTACH:3

ECONOMIC DEVELOPMENT TAX INCENTIVE STUDY - MICROBUSINESS INCOME TAX CREDIT

Pursuant to North Dakota Century Code Section 54-35-26, created by 2015 Senate Bill No. 2057, a variety of economic development tax incentives are to be reviewed by a Legislative Management interim committee over the ensuing six-year period. The study is aimed at ensuring that economic development tax incentives are serving their intended purposes in a cost-effective and equitable manner. This memorandum has been provided to assist in the review of the microbusiness income tax credit and provides an explanation of the incentive, the perceived goals of the Legislative Assembly in creating or altering the incentive, and the data and testimony that will be required to conduct an effective analysis of the incentive.

EXPLANATION OF THE MICROBUSINESS INCOME TAX CREDIT

Section 57-38-01.27 provides for a microbusiness income tax credit. The credit is available to all income taxpayers certified by the Director of the Department of Commerce's Division of Economic Development and Finance as a microbusiness. A taxpayer may claim as a credit 20 percent of the cost of the taxpayer's new investment and new employment in the microbusiness during the taxable year. Credit amounts exceeding a taxpayer's liability may be carried forward to each of the five succeeding taxable years but a taxpayer is limited to claiming no more than \$10,000 in credits over any combination of taxable years. A passthrough entity entitled to the credit must be considered the taxpayer for purposes of the credit and the amount of credit allowed must be determined at the passthrough entity level.

For purposes of Section 57-38-01.27, "new investment" means the amount by which a taxpayer's purchases of microbusiness buildings and depreciable personal property have increased over the amount purchased in the prior year and "new employment" means the amount by which employee compensation payments to North Dakota residents have increased over the amount paid to North Dakota residents in the prior year. The definition of new investment does not include the cost of any registered vehicles and the definition of new employment does not include any merit-based or equity-based salary increases, cost-of-living adjustments, or any other increases in compensation not directly related to the hiring of new employees. In determining the amount of the investment in property when the taxpayer is leasing, rather than purchasing property, the cost of the investment for purposes of calculating the credit is determined by multiplying the increase in average net annual rents by the number of years for which the lease is executed, but not exceeding 10 years.

A business must have fewer than six employees and be located within an economically viable small community to be certified as a microbusiness. An economically viable small community is defined as a community with a population of fewer than 2,000, but no less than 100, and which has an active community economic development organization, an ongoing relationship with a regional or urban economic development organization, or an existing city sales tax for which at least part of the revenues are dedicated to economic development. To apply for certification as a microbusiness, an application must be submitted providing a description of the microbusiness, the projected income and expenditures of the microbusiness, the market to be served by the microbusiness, the way the expansion of the microbusiness addresses market needs, the amount of projected new investment or employment increases created by the microbusiness, projected improvements in income or the anticipated creation of new jobs in the area in which the microbusiness is located, the extent of the applicant's engagement in the microbusiness, and any other information required by the Department of Commerce.

The Department of Commerce may certify a business as a microbusiness if the applicant is, or will be, actively engaged in the operations of the microbusiness; the applicant will create new employment or make a new investment in the microbusiness; the applicant's investments will create new income or jobs in the area in which the microbusiness is located; the microbusiness will not directly compete with any established businesses located within 15 miles of the proposed microbusiness; the microbusiness will be located in an economically viable small community and at least 15 miles from a city with a population of 2,000 or more; and the applicant is not closing or reducing its business operations in one area of the state and relocating substantially the same business operation to another area of the state. The Department of Commerce is required to issue a certification letter to qualifying microbusinesses stating the effective date of the certification but is limited to certifying no more than 200 microbusinesses. The taxpayer must attach the certification letter when applying for the credit.

The Tax Commissioner is required to provide a report to the Department of Commerce identifying the aggregate amount of the tax credit claimed during the previous calendar year and the actual amount of new investment and new employment reported by taxpayers certified as a microbusiness for the previous calendar year. The report must be provided by January 15th of each year and may not contain information protected by state or federal confidentiality laws.

PERCEIVED GOALS OF THE LEGISLATIVE ASSEMBLY IN CREATING OR ALTERING THE MICROBUSINESS INCOME TAX CREDIT

Section 57-38-01.27, providing for a microbusiness income tax credit, was created through the passage of 2007 House Bill No. 1403. The bill provided for an individual and corporate income tax credit equal to 20 percent of new investment and new employment in a microbusiness, which was defined as a business employing five or fewer employees inside an economically viable small community. Upon a review of the legislative history pertaining to House Bill No. 1403, the perceived goal of the Legislative Assembly in creating this credit was to provide an incentive to encourage small businesses to locate and expand in smaller communities. The credit was viewed as a tool to help stimulate rural economies. The estimated fiscal effect of the microbusiness income tax credit could not be determined during the 2007 legislative session, but the maximum lifetime impact of the credit was determined to be \$2 million as each taxpayer was limited to claiming no more than \$10,000 in credits. The Department of Commerce was limited to certifying no more than 200 businesses as qualifying microbusinesses.

The only other changes impacting Section 57-38-01.27 occurred through the passage of 2009 House Bill No. 1324 which served to eliminate the optional long-form filing method (Form ND-2) and replace it with a simplified filing method for any taxpayer who did not have any tax deductions or credits, and through the passage of 2013 House Bill No. 1106. House Bill No. 1106 served to streamline the lengthy description of a passthrough entity by providing a definition of the term at the outset of the income tax chapter.

DATA AND TESTIMONY REQUIRED TO CONDUCT AN EFFECTIVE ANALYSIS OF THE MICROBUSINESS INCOME TAX CREDIT

The interim Political Subdivision Taxation Committee identified various items of data and testimony that would need to be collected to effectively analyze the microbusiness income tax credit. The following list identifies the information the committee sought to collect and the receipt of that information throughout the course of the 2015-16 interim.

1. The number of claimants and the fiscal impact of the incentive.
 - Information (Appendix A) provided to the Political Subdivision Taxation Committee by the Tax Department on December 2, 2015, indicated the total amount of the credit claimed on individual income tax returns in tax years 2007 through 2014 cannot be disclosed due to confidentiality restrictions as the credit was claimed on less than five returns in each tax year.
 - The credit was not claimed on any corporate income tax returns in tax years 2007 through 2014.
2. The use of similar incentives in other states.
 - Incentives similar to this state's microbusiness income tax credit (Appendix B) were found in 13 other states.
3. Employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive.
 - The committee has not identified any employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive as the incentive has been claimed by very few taxpayers in the last several years.
4. Negative impacts created as a result of the incentive.
 - The committee has not identified any negative impacts created as a result of the incentive as the incentive has been claimed by very few taxpayers in the last several years.
5. Benefits that flow to out-of-state concerns resulting from the incentive.
 - The committee has not identified any benefits that flow to out-of-state concerns resulting from the incentive as the incentive has been claimed by very few taxpayers in the last several years.
6. Testimony from interested parties.
 - Testimony has not been received from parties in support of retaining the microbusiness income tax credit.
 - Testimony (Appendix C) was provided by the Economic Development Association of North Dakota in support of eliminating the microbusiness income tax credit.

ATTACH:3

ECONOMIC DEVELOPMENT TAX INCENTIVE STUDY - CERTIFIED NONPROFIT DEVELOPMENT CORPORATION INVESTMENT CREDIT

Pursuant to North Dakota Century Code Section 54-35-26, created by 2015 Senate Bill No. 2057, a variety of economic development tax incentives are to be reviewed by a Legislative Management interim committee over the ensuing six-year period. The study is aimed at ensuring that economic development tax incentives are serving their intended purposes in a cost-effective and equitable manner. This memorandum has been provided to assist in the review of the certified nonprofit development corporation investment credit and provides an explanation of the incentive, the perceived goals of the Legislative Assembly in creating or altering the incentive, and the data and testimony that will be required to conduct an effective analysis of the incentive.

EXPLANATION OF THE CERTIFIED NONPROFIT DEVELOPMENT CORPORATION INVESTMENT CREDIT

Sections 10-33-124 and 57-38-01.17 provide for a certified nonprofit development corporation investment credit. The income tax credit is available to corporate income taxpayers in an amount equal to 25 percent of the amount paid for dues, membership fees, or contributions to a certified nonprofit development corporation. A taxpayer may claim no more than \$2,000 in credits over any combination of taxable years and may carry forward any unused credits for up to seven taxable years. The credit is not available to subchapter S corporations.

To become certified as a nonprofit development corporation, a corporation must apply to the Secretary of State, invest the majority of its funds in a primary sector business, and may not distribute any part of its income to its members, directors, or officers. For purposes of the credit, a primary sector business is a business that adds value to a product produced for resale through a process employing knowledge and labor. A certified nonprofit development corporation must file a form with the Tax Commissioner identifying each contributing taxpayer and the amount remitted within 30 days of receiving taxpayer funds. The certified nonprofit development corporation must also file two copies of this form with the contributing taxpayer. The contributing taxpayer is then required to attach one copy of this form to the taxpayer's income tax return in order to claim the credit.

PERCEIVED GOALS OF THE LEGISLATIVE ASSEMBLY IN CREATING OR ALTERING THE CERTIFIED NONPROFIT DEVELOPMENT CORPORATION INVESTMENT CREDIT

The certified nonprofit development corporation investment credit was first enacted through the passage of 1989 House Bill No. 1558. The provisions contained in the bill were substantially similar to the provisions found in current law. The only notable difference between the law as it currently reads and the law as originally enacted was the scope of application. In its original form, the credit could be claimed by individuals, estates, and trusts filing the optional long-form tax return and taxpayers filing corporate income tax returns. In its current form, the credit can only be claimed by corporate income taxpayers. Upon a review of the legislative history pertaining to the bill, the perceived goal of the Legislative Assembly in creating this credit was to provide an incentive for taxpayers to pool their resources and invest in economic development within their communities. The estimated fiscal effect of the certified nonprofit development corporation investment credit could not be determined during the 1989 legislative session.

The only other changes to the credit occurred in during the 1997 and 2009 legislative sessions. The passage of 1997 Senate Bill No. 2210 served primarily as the means to rewrite an updated version of the Nonprofit Corporations Act within the newly created Chapter 10-33. The bill also added various reporting requirements to the certified nonprofit development corporation investment credit and eliminated the ability of a subchapter S corporation to claim the credit. The most recent changes to the credit occurred as a result of 2009 House Bill No. 1324, which eliminated the optional long-form filing method (Form ND-2), which was the only method the credit could be claimed by individuals.

DATA AND TESTIMONY REQUIRED TO CONDUCT AN EFFECTIVE ANALYSIS OF THE CERTIFIED NONPROFIT DEVELOPMENT CORPORATION INVESTMENT CREDIT

The interim Political Subdivision Taxation Committee identified various items of data and testimony that would need to be collected to effectively analyze the certified nonprofit development corporation investment credit. The following list identifies the information the committee sought to collect and the receipt of that information throughout the course of the 2015-16 interim.

1. The number of claimants and the fiscal impact of the incentive.
 - Information (Appendix A) provided to the Political Subdivision Taxation Committee by the Tax Department on December 2, 2015, indicated the credit was not claimed on any corporate income tax returns in tax years 2006 through 2014.
2. The use of similar incentives in other states.
 - Incentives similar to this state's certified nonprofit development corporation investment credit (Appendix B) were found in eight other states.
3. Employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive.
 - The committee has not identified any employment opportunities, business growth, or diversity in the state's economy resulting from the availability of the incentive as the incentive has not been claimed by any taxpayers in the last several years.
4. Negative impacts created as a result of the incentive.
 - The committee has not identified any negative impacts created as a result of the incentive as the incentive has not been claimed by any taxpayers in the last several years.
5. Benefits that flow to out-of-state concerns resulting from the incentive.
 - The committee has not identified any benefits that flow to out-of-state concerns resulting from the incentive as the incentive has not been claimed by any taxpayers in the last several years.
6. Testimony from interested parties.
 - Testimony has not been received from parties in support of retaining the certified nonprofit development corporation investment credit.
 - Testimony (Appendix C) was provided by the Economic Development Association of North Dakota in support of eliminating the certified nonprofit development corporation investment credit.

ATTACH:3

3/1/2017

HB 1044

Attachment #1

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Prepared for the Political Subdivision Taxation Committee

STATUTORY DEFINITIONS OF PRIMARY SECTOR BUSINESS

This memorandum was requested by the interim Political Subdivision Taxation Committee to compare the various ways a primary sector business is defined throughout the North Dakota Century Code.

The phrase "primary sector business" is defined in nine separate instances throughout Century Code. The most commonly used components found in the definitions of primary sector business include components defining a primary sector business as:

1. An individual, corporation, limited liability company, partnership, or association;
2. Which through the employment of knowledge or labor adds value to a product, process, or service;
3. That results in the creation of new wealth.

A definition containing only these three components is found in Section 40-57.1-02, pertaining to tax exemptions for new and expanding businesses, which provides:

3. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association which through the employment of knowledge or labor adds value to a product, process, or service that results in the creation of new wealth.

Nearly identical definitions can be found in Sections 26.1-50-01, 57-39.2-04.3, and 57-38-01.33. These sections contain all three components, with the additional requirement that the business's status as a primary sector business be certified by the Department of Commerce. Any deviations in the language found in these three sections from the language found in Section 40-57.1-02 have been offset in bold below.

Section 26.1-50-01, pertaining to the North Dakota low-risk incentive fund, provides:

4. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association that through the employment of knowledge or labor adds value to a product, process, or service which results in the creation of new wealth. **Qualification as a primary sector business under this subsection must be determined by the department of commerce division of economic development and finance. (emphasis supplied)**

Section 57-39.2-04.3, pertaining to a sales tax exemption for primary sector business computer and telecommunications equipment, provides:

- g. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association that through the employment of knowledge or labor adds value to a product, process, or service which results in the creation of new wealth **and which has been certified by the department of commerce division of economic development and finance to be qualified under this subdivision. (emphasis supplied)**

Section 57-38-01.33, pertaining to an income tax credit for purchasing manufacturing machinery and equipment to automate a manufacturing process, provides:

- b. "Primary sector business" means **a business certified by the department of commerce** which, through the employment of knowledge or labor, adds value to a product, process, or service that results in the creation of new wealth. **(emphasis supplied)**

Definitions of a primary sector business in Sections 10-33-124 and 57-38-30.5 lack the final component of the definition provided in Section 40-57.1-02 associated with the creation of new wealth. The definition in Section 10-33-124 only pertains to adding value to a product produced for resale, rather than a product, process, or service. Any deviations in the language found in these two sections from the language found in Section 40-57.1-02 have been offset in bold below.

Section 10-33-124, pertaining to certified nonprofit development corporations, provides:

- b. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association that, through a process employing knowledge and labor, adds value to a **product produced for resale. (emphasis supplied)**

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Section 57-38-30.5, pertaining to the income tax credit for research and experimental expenditures, provides:

- c. "Primary sector business" means **a qualified business** that through the employment of knowledge or labor adds value to a product, process, or service. **(emphasis supplied)**

The final three definitions of a primary sector business are found in Sections 10-30.5-01, 57-38.5-01, and 52-02.1-01 and either add or omit certain types of businesses or facilities from the definition of a primary sector business or add additional eligibility criteria. Any deviations in the language found in these three sections from the language found in Section 40-57.1-02 have been offset in bold below.

Section 10-30.5-01, pertaining to the North Dakota Development Fund, provides:

4. "Primary sector business" means an individual, corporation, limited liability company, partnership, or association which through the employment of knowledge or labor adds value to a product, process, or service that results in the creation of new wealth. **The term includes tourism but does not include production agriculture. (emphasis supplied)**

Section 57-38.5-01, pertaining to the seed capital investment tax credit, provides:

4. "Primary sector business" means **a qualified business** that through the employment of knowledge or labor adds value to a product, process, or service and which results in the creation of new wealth **but does not include an agricultural commodity processing facility as defined under section 57-38.6-01. (emphasis supplied)**

The definition of "qualified business" in Section 57-38.5-01 requires a business to be incorporated as a corporation, passthrough entity, or joint venture.

Section 52-02.1-01, pertaining to the new jobs training program, provides:

11. "Primary sector business" means **an employer engaged in locating to or in this state which previously had no presence in this state, or in expanding its operations within this state,** which through the employment of knowledge or labor, adds value to a product, process, or export service that results in the creation of new wealth, **excluding production agriculture, if it meets the following eligibility criteria:**
 - a. **An employer entering into an agreement, and increasing its base employment level by at least one employee, or in the case of an employer without an established base employment level in this state creating at least five employees, within the time set in the agreement, is entitled to the new jobs credit from withholding.**
 - b. **An employer must have an economically productive and socially desirable purpose within the state.**
 - c. **An employer must not be closing or reducing its operation in one area of the state and relocating substantially the same operation in another area. (emphasis supplied)**

CONCLUSION

Though some variations exist among the nine separate definitions for a primary sector business within Century Code, many common elements are shared by them. The main differences tend to center around whether a business must be certified by the Department of Commerce; whether the addition of value to a product, process, or service must result in the creation of new wealth; and the types of entities that are included in or excluded from the definition of a primary sector business for purposes of the incentive being applied.