

FISCAL NOTE
Requested by Legislative Council
12/20/2016

Bill/Resolution No.: HB 1050

- 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.*

	2015-2017 Biennium		2017-2019 Biennium		2019-2021 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.*

	2015-2017 Biennium	2017-2019 Biennium	2019-2021 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).*

HB 1050 repeals the microbusiness income 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.*

Section 3 of HB 1050 repeals the microbusiness income tax credit. If enacted, HB 1050 is expected to have no fiscal impact as this tax credit has not been utilized in any recent tax years.

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.*

- 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: 701.328.3402

Date Prepared: 01/02/2017

2017 HOUSE FINANCE AND TAXATION

HB 1050

2017 HOUSE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Fort Totten Room, State Capitol

HB 1050
1/4/2017
26530

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature

Mary Brucker

Explanation or reason for introduction of bill/resolution:

A bill relating to the list of economic development tax incentives subject to regular review and the application of tax credits against individual income tax liability and relating to the microbusiness income tax credit.

Minutes:

Attachment #1

Chairman Headland: Opened hearing.

Vice Chairman Dockter: Introduced bill. The intent of this credit was first enacted in 2007. The goal of the credit was to provide an incentive to encourage small businesses to expand in smaller communities. The credit was being used as a tool to help stimulate rural economies. The credit was claimed on less than five individual income tax returns in tax years 2007-2014. The committee did not receive any support for continuation of any microbusiness income tax credit.

Chairman Headland: Any questions for Vice Chairman Dockter?

Emily Thompson, Counsel, Legislative Council: This credit provides a credit to both individual income taxpayers and corporate income taxpayers. The amount of the credit is equal to 20% of the cost of a taxpayer's new investment and new employment in a microbusiness during the taxable year. The lifetime cap for this credit is \$10,000 per taxpayer. New investment is defined as the amount of which the taxpayer's purchases of microbusiness buildings and property has increased over the amount purchased in the prior year. New employment means the amount by which employee compensation payments to North Dakota residents has increased over the amount paid to those same North Dakota residents in the prior year. That is what we're looking at when we're talking about 20% of the costs of a taxpayer's new investment and new employment. The credit has been used very infrequently; less than five claimants from enactment through 2014 on the individual income tax side and no claimants from enactment through 2014 on the corporate income tax side. In the survey of other states that used this credit it was a broad survey for credits that had a similar function. The North Dakota credit is rather specific which might be one of the factors that leads to it being relatively underutilized. A business must have fewer than six employees and must be located within an economically viable small community which is

defined as a community whose population ranges from 100-1,999. To be certified as a microbusiness the applicant must submit information describing the microbusiness, the business' projected income and expenditures, what the business will do to address market needs, the amount of projected new investment and new employment, and any other information the Department of Commerce requires. The microbusiness may not be certified by the Department of Commerce if it directly competes with any established business located within 15 miles of the applicant. The applicant may not simply be closing or reducing their business operations in one area of the state and then relocating the same business operation to another area of the state. The first section of the bill draft is simply removing the specific credit from the list of those incentives that are to be studied over that three interim period. The second section of the bill is the individual income tax imposition section of the code and it contains a listing of all the different credits a taxpayer may claim. Section three is to repeal and Section four is the effective date for taxable years beginning after December 31, 2016. There is no fiscal impact to this repeal as the credit has not been claimed.

Chairman Headland: Were there any restrictions associated with any type of business that could qualify? I'm just trying to figure out why the credit wasn't used. I don't recall from the interim committee if we got any testimony as to why.

Emily Thompson, Counsel, Legislative Council: I don't believe we received any testimony from parties supporting the credit. The only testimony we received was from the Economic Development Association of North Dakota. They were in support of eliminating this credit because it was not used. I don't know if there are certain businesses that are restricted from being one type of business or another.

Chairman Headland: If you had a small town that didn't have a café but they wanted to start one and they qualified is there a reason why the Department of Commerce wouldn't have certified them?

Emily Thompson, Counsel, Legislative Council: I will defer to the Department of Commerce on that since they are the agency that certifies microbusinesses.

Justin Dever, Co-Deputy Commissioner at the North Dakota Department of Commerce: The only real limitation is the competition. As long as there is not a competing business within 15 miles they would be eligible for this type of tax credit.

Chairman Headland: The 15-mile constraint would possibly cause some issues which may be why it didn't get used.

Representative Ertelt: Would these similar businesses be eligible for the new and expanding business income tax exemption and is that maybe why they didn't use this credit?

Justin Dever: I don't believe so but I'm not sure. The tax department may be able to see if they are eligible or not. These are intended to be smaller companies. One of the requirements is that a microbusiness will employ five or fewer employees. I'm not sure they would even go through the process even if they were eligible to receive the five-year exemption. The newer expanding business also requires primary sector certification so some of these small town businesses would not qualify.

Representative Grueneich: What does primary sector mean?

Justin Dever: We'll go in much greater depth on the definition of primary sector definition on the next bill. It basically means that a business is adding value and creating new wealth. Instead of recycling wealth that is already in the area it is bringing in the new wealth.

Chairman Headland: Any other questions? Is there support of HB 1050?

Jennifer Greuel, Executive Director of Economic Development Association of North Dakota: We are in support. See attachment #1.

Chairman Headland: Any other testimony in support? Is there any opposition to HB 1050? Does anyone have any questions for the Tax Department?

Joe Becker, North Dakota Tax Department: The new and expanding business incoming exemption requires primary sector or it has to be in tourism.

Chairman Headland: Thank you for making that clarification.

Representative Ertelt: In your estimation, businesses that would qualify for the microbusiness income tax credit would not qualify for the new and expanding income tax exemption?

Joe Becker: I wouldn't say that categorically. The sort of business has to sell product outside the state as a general rule. That can happen in small towns so it is not ruled out.

Chairman Headland: Any further questions? I will close the hearing on HB 1050. I would entertain a motion.

Representative B. Koppelman: Made a motion for a Do Pass.

Representative Olson: Seconded.

Chairman Headland: Is there any committee discussion? I believe the 15-mile parameter probably precluded it from being used in a lot of cases. However, if it had been expanded or if that particular part of it was narrowed down to something smaller than that you may see such broad use of it that it could impact the budget in such a way that we may not want to look at it right now. It was put into effect at a time where we were trying to generate some things in rural America and maybe oil helped us with that without fully utilizing the credits. I agree with the Do Pass motion.

ROLL CALL VOTE: 14 YES 0 NO

MOTION CARRIED

REPRESENTATIVE HOWE WILL CARRY THIS BILL

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

2017 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1050

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. Koppelman Seconded By Rep. Olson

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	✓				

Total (Yes) 14 No 0

Absent 0

Floor Assignment Rep. Howe

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

REPORT OF STANDING COMMITTEE

HB 1050: Finance and Taxation Committee (Rep. Headland, Chairman) recommends **DO PASS** (14 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1050 was placed on the Eleventh order on the calendar.

2017 SENATE FINANCE AND TAXATION

HB 1050

2017 SENATE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Lewis and Clark Room, State Capitol

House Bill 1050
3/7/2017
Job #: 28791

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature

Jana Bellamy

Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact subsection 3 of section 54-35-26 and subsection 7 of section 57-38-30.3 of the North Dakota Century Code, relating to the list of economic development tax incentives subject to regular review and the application of tax credits against individual income tax liability; to repeal section 57-38-01.27 of the North Dakota Century Code, relating to the microbusiness income tax credit; and to provide an effective date.

Minutes:

Attachment #1

All Senators present.

Chairman Cook: Opened the public hearing on HB 1050.

Representative Jason Dockter, District 7: During the last interim studied some of the economic incentives. One of them that came up is microbusiness credit. As the bill states, we want to repeal this credit due to lack of usage. Never really been used.

Emily Thompson, Legal Counsel, Legislative Council: Handed out attachment #1. Gave a quick summary of the tax credit and the changes being suggested in the bill.

Closed the hearing on HB 1050.

2017 SENATE STANDING COMMITTEE MINUTES

Finance and Taxation Committee Lewis and Clark Room, State Capitol

House Bill 1050
3/8/2017
Job #: 28905

- ☐ Subcommittee
☐ Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

A BILL for an Act to amend and reenact subsection 3 of section 54-35-26 and subsection 7 of section 57-38-30.3 of the North Dakota Century Code, relating to the list of economic development tax incentives subject to regular review and the application of tax credits against individual income tax liability; to repeal section 57-38-01.27 of the North Dakota Century Code, relating to the microbusiness income tax credit; and to provide an effective date.

Minutes:

No Attachments

All Senators present.

Chairman Cook: Committee work on HB 1050.

Vice Chairman Bekkedahl move a do pass on HB 1050.

Senator Laffen seconded.

Senator Unruh: I know we investigated this a lot in the interim and it is important for us to repeal it.

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

Motion carries.

Senator Laffen will carry the bill.

Date:

3/8

Roll Call Vote #: 1

2017 SENATE STANDING COMMITTEE ROLL CALL VOTES

BILL/RESOLUTION NO. 1050

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. Laffen

Senators	Yes	No	Senators	Yes	No
Chairman Dwight Cook	<input checked="" type="checkbox"/>		Senator Jim Dotzenrod	<input checked="" type="checkbox"/>	
Vice Chair Brad Bekkedahl	<input checked="" type="checkbox"/>				
Senator Lonnie J. Laffen	<input checked="" type="checkbox"/>				
Senator Jessica Unruh	<input checked="" type="checkbox"/>				
Senator Scott Meyer	<input checked="" type="checkbox"/>				

Total (Yes) 6 No 0Absent 0Floor Assignment Sen. Laffen

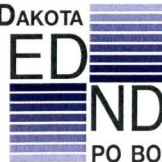
If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1050: Finance and Taxation Committee (Sen. Cook, Chairman) recommends **DO PASS** (6 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING). HB 1050 was placed on the Fourteenth order on the calendar.

2017 TESTIMONY

HB 1050



**Testimony of Jennifer Greuel, Executive Director
Economic Development Association of North Dakota (EDND)
In Support of HB 1048, 1049 and 1050
January 4, 2017**

Chairman and members of the House Finance and Taxation Committee:

The Economic Development Association of North Dakota represents more than 80 large and small and rural and urban economic development organizations on the front line of growing businesses and communities in North Dakota. The primary purpose of the organization is to support the creation of new wealth and the diversification of North Dakota's economy.

EDND stands before you in support of the eliminating the Certified Nonprofit Development Corporation Investment Credit (HB 1048), the Wage and Salary Credit (HB 1049), and the Microbusiness Income Tax Credit (HB 1050) due to the lack of use and limited scope of each.

Economic development tax incentives can be important tools in supporting entrepreneurship, innovation and start-up companies in the state, which is critical to diversifying North Dakota's economy. North Dakota no longer simply competes with other states, but rather on a global scale. Properly structured tax incentives can help companies meet the challenges facing businesses today.

EDND would like to thank you for your commitment to review all incentives and adjust or enhance incentives accordingly, as would most benefit the state. Our organization has been supportive of your efforts to demonstrate the value of the state's investment in business support programs to grow and diversify North Dakota's economy. We were very active in the interim study process because we too want to assure North Dakota taxpayers these investments provide a return on their investment.

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1-4-17

Thank you for the opportunity to address the committee and express support for these bills and your continued commitment to keeping North Dakota globally competitive to recruit and retain viable businesses.

3/7/2017

HB 1050

Attachment #1

pg 1

17.9088.04000

Prepared for the Political Subdivision Taxation Committee

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.

3/9/2017

HB 1050

#1

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