



Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873
Email: fiscal.bureau@legis.wisconsin.gov • Website: <http://legis.wisconsin.gov/lfb>

2017

Joint Committee on Finance

Paper #297

Reallocate Early Stage Business Investment Credits to the Business Development Tax Credit (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2017-19 Budget Summary: Page 184, #20]

CURRENT LAW

Early Stage Business Investment Credits. The early stage business investment program includes two nonrefundable tax credits: (a) the angel investment credit, which can be claimed under the individual income tax; and (b) the early stage seed investment credit, which can be claimed under the individual income tax, the corporate income/franchise tax, and the insurance premiums tax. The angel investment credit equals 25% of the claimant's bona fide angel investment made directly in a qualified new business venture (QNBV) certified by the Wisconsin Economic Development Corporation (WEDC). The early stage seed investment credit is equal to 25% of the claimant's investment paid to a certified fund manager that the fund manager invests in a QNBV. For purposes of this paper, the two credits are jointly referred to as "investment credits."

The annual limit on the amount of investment credits that can be verified by WEDC is \$30 million per calendar year. If less than \$30 million in investment credits are verified by WEDC in a given year, WEDC can request a reallocation of unused investment credits in the current calendar year to increase the credit amount that can be allocated under the refundable business development credit in that year. The proposed reallocation is subject to a 14-day passive review by the Joint Committee on Finance. The nonrefundable investment credits are recorded as revenue reductions under the state accounting system, rather than expenditures.

Prior to the creation of WEDC in 2011, the investment credits were administered by the Department of Commerce.

Business Development Credit. A refundable credit can be claimed against the individual

income tax and the corporate income/franchise tax equal to a portion of certain costs incurred by businesses related to eligible wages paid to employees, investment expenses, and job training expenses. Under the state accounting system, refundable business development credits are treated as expenditures (rather than revenue offsets) and are paid from a GPR sum sufficient appropriation. In order for a person to be certified to receive the credit, that person must operate or intend to operate a business in the state and enter into a contract with WEDC. Certifications can remain in effect for up to 10 years. WEDC was authorized to allocate up to \$17 million of business development credits in calendar year 2016 and may authorize up to \$22 million annually thereafter. Any unused allocation can be carried forward to allocate in future years.

The business development credit was created under 2015 Wisconsin Act 55, which consolidated aspects of the nonrefundable economic development credit and the refundable jobs credit. Act 55 sunset the jobs and economic development credits for taxable years beginning after December 31, 2015, and the business development credit took effect for taxable years beginning in 2016. As noted, unused investment credits can be reallocated to the business development credit, subject to a 14-day passive review by the Committee. Prior to 2016, WEDC could request a reallocation of credits under the same process for the refundable jobs credit.

GOVERNOR

Permit WEDC to request a reallocation of nonrefundable investment credits that were unused in the immediately preceding calendar year, rather than credits that are unused in the current calendar year, to the refundable business development credit.

DISCUSSION POINTS

1. The early stage business investment program was enacted under 2003 Wisconsin Act 255, and has been amended multiple times since then. Act 255 initially imposed annual limits on the amount of each credit that could be verified (\$3 million for the angel credit and \$3.5 million for the early stage seed credit). These individual limits were increased several times and then combined into the current \$30 million limit under 2015 Act 55, beginning in 2015. The only year in which one of the limits was nearly reached was in 2005, when the number of angel credits verified was \$10,000 less than the statutory limit for that year.

2. Table 1 shows information regarding usage of the credits since 2005. From 2005 through 2016, utilization of the investment credits has been approximately 42% of the aggregate annual statutory limit, and credit awards have not exceeded 76% of the aggregate annual statutory limit for the two credits in any calendar year. Data shown for 2016 is preliminary and may be subject to change.

TABLE 1**Investment Credits Verified by WEDC/Commerce**

<u>Year</u>	<u>Angel Credits</u>	<u>Early Stage Seed Credits</u>	<u>Total Credits</u>	<u>Aggregate Annual Statutory Limit</u>	<u>Percentage of Annual Limit Utilized</u>
2005	\$2,990,000	\$126,000	\$3,116,000	\$6,500,000	47.9%
2006	2,418,000	1,423,000	3,841,000	6,500,000	59.1
2007	2,050,000	2,600,000	4,650,000	6,500,000	71.5
2008	3,106,000	4,284,000	7,390,000	11,500,000	64.3
2009	5,529,000	3,226,000	8,755,000	11,500,000	76.1
2010	5,032,000	2,567,000	7,599,000	14,500,000	52.4
2011	6,701,000	4,622,000	11,323,000	40,500,000	28.0
2012	8,209,000	3,807,000	12,016,000	40,500,000	29.7
2013	6,025,000	2,803,000	8,828,000	40,500,000	21.8
2014	6,959,000	5,474,000	12,433,000	40,500,000	30.7
2015	12,359,000	5,984,000	18,343,000	30,000,000	61.1
2016*	8,981,000	8,901,000	17,882,000	30,000,000	59.6

*2016 Data is preliminary.

Source: Wisconsin Economic Development Corporation

3. In estimating state tax revenues, this office and the administration must make assumptions regarding the amount of investment credits that will be claimed and used by taxpayers each year. These assumptions are based on the historic utilization rates shown in Table 1. State revenue estimates do not assume that credit payments will equal the statutory limits.

4. Under the 14-day passive review process, the Committee has authorized the reallocation of unused investment credits on several occasions. Commerce/WEDC have submitted six reallocation requests to the Committee, of which five were approved and one was withdrawn after an objection was raised. Table 2 shows the five reallocation requests that were approved. The largest credit reallocation that the Committee has approved was \$10.0 million in 2012.

TABLE 2**Credit Reallocations Approved by the Joint Committee on Finance**

<u>Year</u>	<u>Amount Reallocated</u>
2009	\$3,091,375
2010	6,836,288
2011	7,000,000
2012	10,000,000
2016	<u>8,000,000</u>
Total	\$34,927,663

5. The current reallocation process is based on excess investment credits available in the current year and, therefore, requires WEDC to estimate how many credits will be verified prior to year-end. The Governor's proposal would be based on a known amount of unused credits in the prior year. The Governor's recommendation would provide certainty that WEDC will not underestimate usage of the credits in a given year and be unable to meet demand for the credits later in the year.

6. In the past, the current reallocation procedure, which links the investment credits with the business development credit (and before 2016, the jobs credit), has led to confusion among legislators and other stakeholders who believed that state revenue estimates assumed that the full allocation of investment credits would be verified and claimed each year, and that a reallocation of unused investment credits would not have a state fiscal effect. This confusion could be avoided if the statutory linkage between the investment credits and the business development credit was eliminated. Instead, the statutes could simply allow for an annual supplement to the business development credit, with approval by the Committee under a 14-day passive review process. This option is presented as Alternative 2, with a maximum annual supplement of \$10 million. The \$10 million amount is based on the largest reallocation to-date, as shown in Table 2. Under this option, WEDC would be required to provide evidence as to why the request is necessary to accomplish its statewide economic development objectives.

7. As noted, the business development credit is a refundable credit and, unlike nonrefundable credits, is paid to a claimant regardless of whether the claimant has a state tax liability. As a result, it could be argued that a refundable credit awarded to businesses on a discretionary basis by WEDC is similar to a grant awarded by any state agency. LFB Paper #293 discusses alternatives to convert refundable tax credit programs administered by WEDC, including the business development tax credit program, to grant programs.

ALTERNATIVES

1. Adopt the Governor's recommendation.

2. Delete the provision recommended by the Governor and repeal the current law provision allowing WEDC to request a reallocation of unused investment credits to the business development credit under a 14-day passive review of the Joint Committee on Finance. Instead, permit WEDC to request an increase of up to \$10 million annually to the \$22 million statutory limit for the amount of business development credits that may be may allocated. Require WEDC to provide evidence in its request as to why the request is necessary to accomplish its statewide economic development objectives.

3. Delete the provision recommended by the Governor and maintain current law.

Prepared by: Sean Moran