

Department of Legislative Services
 Maryland General Assembly
 2019 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 117 (Delegate Lafferty)
 Environment and Transportation and
 Ways and Means

Maryland Smart Growth Investment Fund

This bill requires the Department of Commerce (Commerce) to issue a request for proposals (RFP) for a management entity to establish the Maryland Smart Growth Investment Fund as specified. The Governor must appropriate \$7.0 million to the fund in fiscal 2021; however, Commerce is not required to invest the appropriated monies if the committed capital in the fund is less than \$25.0 million on December 31, 2021. **The bill takes effect June 1, 2019.**

Fiscal Summary

State Effect: No effect in FY 2019. General fund expenditures increase by \$0.3 million in FY 2020, \$7.4 million in FY 2021, and about \$0.1 million annually thereafter. Revenues are not affected, as discussed below. **This bill establishes a mandated appropriation for FY 2021.**

(\$ in millions)	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
Revenues	\$0	\$0	\$0	\$0	\$0
GF Expenditure	0.3	7.4	0.1	0.1	0.1
Net Effect	(\$0.3)	(\$7.4)	(\$0.1)	(\$0.1)	(\$0.1)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease

Local Effect: The bill does not directly affect local government finances or operations.

Small Business Effect: None.

Analysis

Bill Summary: The investment fund established by the management entity under the RFP must be (1) based on the recommendations of the 2013 report of the Maryland Smart Growth Investment Fund Workgroup and (2) designed to meet the requirements for a Qualified Opportunity Fund under the federal Tax Cuts and Jobs Act of 2017. To carry out the purposes of the bill, Commerce may create, own, control, or be a member of a corporation, limited liability company, partnership, or any other entity, whether operated for-profit or not-for-profit.

Current Law/Background:

Maryland Smart Growth Investment Fund Workgroup

Chapter 592 of 2013 established the Maryland Smart Growth Investment Fund Workgroup to make recommendations for the design and creation of an investment fund that would encourage and support smart growth in targeted areas. The workgroup included members of the General Assembly, representatives from the Department of Housing and Community Development (DHCD), Commerce, local governments, and the private sector, among others. The workgroup report can be found on the Department of Legislative Services' (DLS) [website](#).

The workgroup recommended that the Maryland Economic Development Corporation (MEDCO) should “sponsor” the fund and act as an intermediary between the State and the private sector. At the time, MEDCO agreed to develop a plan for the creation of the fund and to select a fund manager and to determine investment criteria. However, according to MEDCO, the fund was not established. MEDCO advises that this was due to DHCD deciding to use internal funds, as discussed below.

The *2017 Joint Chairmen’s Report* (page 164) asked DHCD to provide information related to why the fund had not been established. DHCD’s response to that request indicated that DHCD had “met the programmatic intent” of the Maryland Smart Growth Investment Fund Workgroup by establishing the Neighborhood Business Loan Program under its expanded Neighborhood Business Works Program authority. The program provides loans for business lending projects funded through a combination of private capital sourced by the Community Development Administration in DHCD and State special and general obligation bond funds. The DHCD response can be found on the DLS [website](#).

Opportunity Zones

The Federal Tax Cuts and Jobs Act of 2017 established the Qualified Opportunity Zones Program to incentivize private investment in distressed communities. Under the Act, states

may nominate up to 25% of specified low-income census tracts for designation by the U.S. Treasury as Opportunity Zones. Maryland designated zones in 2018, as shown in the **Appendix – Maryland Qualified Opportunity Zones**. The Administration has also established the [Opportunity Zone Leadership Task Force](#) by executive order to provide guidance and coordinate efforts related to Opportunity Zone investment.

A qualified Opportunity Fund is a privately managed investment vehicle organized as a corporation or a partnership for the purpose of investing in qualified Opportunity Zone property and that holds at least 90% of its assets in such property. Qualified Opportunity Zone property includes stock, a partnership interest, and tangible property used in a trade or business.

The program offers three federal tax incentives related to capital gains: (1) a temporary tax deferral for capital gains reinvested in an Opportunity Fund; (2) a step up in basis for capital gains reinvested in an Opportunity Fund, which excludes up to 15% of the original capital gain from taxation; and (3) a permanent exclusion from taxable income of capital gains from the sale or exchange of an investment in an Opportunity Fund, if the investment is held for at least 10 years. More information on the tax incentives, including helpful illustrative examples, can be found on the Economic Innovation Group’s [website](#).

State Fiscal Effect: General fund expenditures increase by \$336,229 in fiscal 2020, which reflects a four-month start-up delay. This estimate reflects the cost of hiring one contract manager to oversee the RFP process and provide related, ongoing oversight. It includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses. It also includes \$250,000 for the management entity hired by Commerce to establish the fund, an estimate based on Commerce’s previous experience with hiring a vendor to assist with setting up the tax credit sale for the InvestMaryland program, and the likely timing of such expenditures.

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Salary and Fringe Benefits	\$80,870
Fund’s Management Entity	250,000
Operating Expenses	<u>\$5,359</u>
Total FY 2020 State Expenditures	\$336,229

Future year expenditures reflect a full salary with annual increases and employee turnover and ongoing operating expenses. Fiscal 2021 expenditures also reflect an additional \$250,000 for the fund’s management entity and the \$7.0 million mandated appropriation.

Although the bill requires the Maryland Smart Growth Investment Fund to be established, it does not establish the fund as a special fund in statute. This analysis assumes that the fund is not a budgeted special fund, nor is it considered a “nonbudgeted fund” for purposes

of the annual State budgeting process. To the extent that this is not the case, State nonbudgeted revenues and expenditures increase to reflect the receipt and expenditure of general fund appropriations and, as contemplated by the bill, at least \$25.0 million received from investors.

In future years, if there is sufficient money in the fund, a portion of the fund's earnings may be able to be used to pay for Commerce's annual expenditures associated with its oversight role. This has not been reflected in the above estimates.

Additional Comments: [Regulations](#) released by the Internal Revenue Service require that mixed funds (*i.e.*, not entirely capital gains) in an Opportunity Fund be treated as two separate investments. For those investments not comprising capital gains, the related federal tax incentives described above do not apply.

Additional Information

Prior Introductions: SB 632 of 2018, a similar bill as amended, had a conference committee appointed, but no further action was taken. Its cross file, HB 817, received a hearing from the House Appropriations Committee, but no further action was taken.

Cross File: SB 3 (Senator Rosapepe) - Finance.

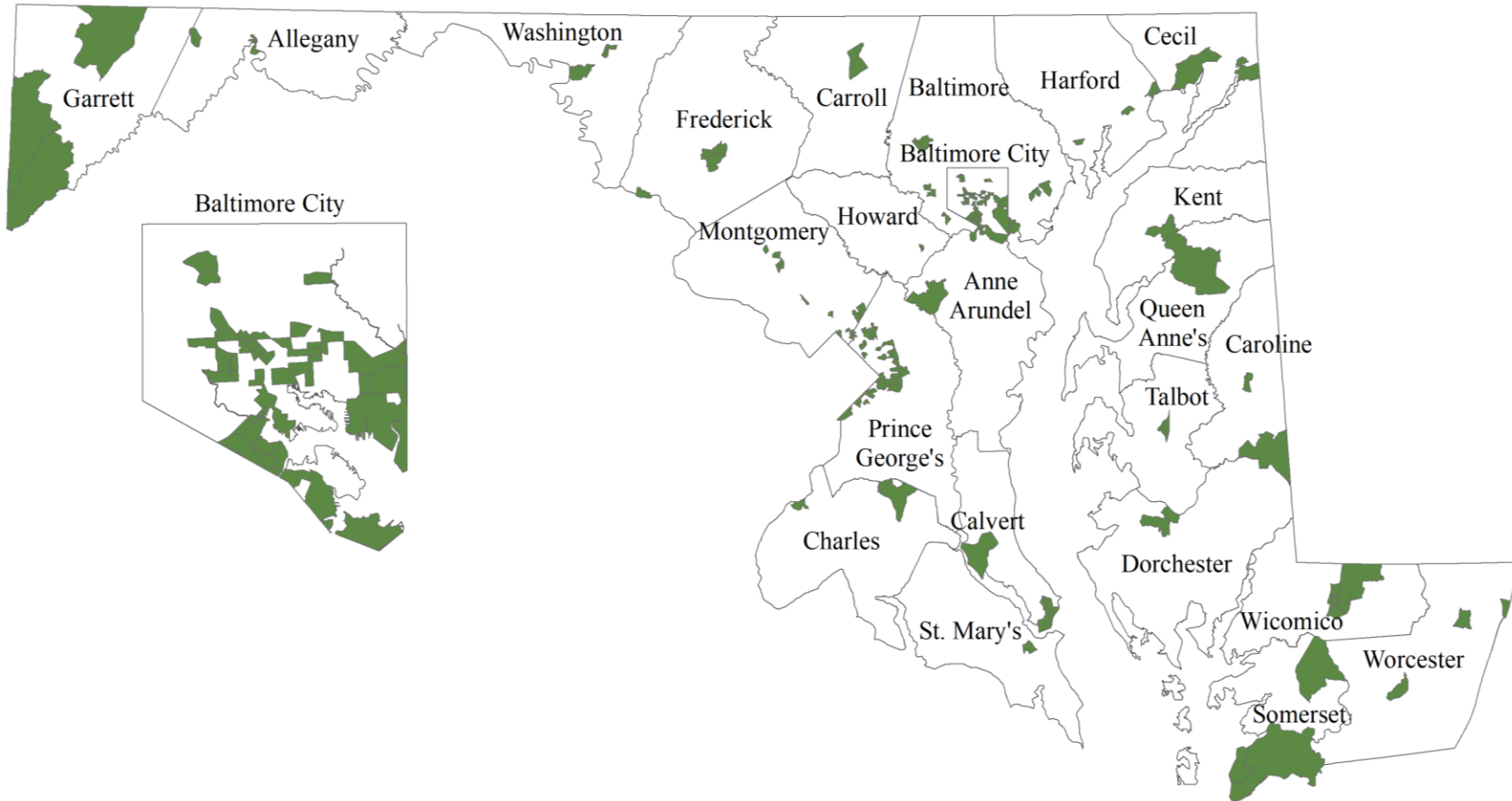
Information Source(s): Department of Commerce; Department of Housing and Community Development; Maryland Economic Development Corporation; Department of Information Technology; Internal Revenue Service; Economic Innovation Group; Department of Legislative Services

Fiscal Note History: First Reader - January 24, 2019
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Appendix – Maryland Qualified Opportunity Zones



Source: Department of Information Technology (MD iMAP)