Department of Legislative Services
Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE
Revised

House Bill 1289 (Chair, Ways and Means Committee)(By Request - Departmental - Business and Economic Development)

Ways and Means Budget and Taxation

Economic Development - Qualified Distressed Counties - One Maryland Economic Development Tax Credit

This departmental bill alters the definition of "qualified distressed county" to include counties with unemployment rates at least two percentage points higher than the State average. It also authorizes qualified business entities to claim a prorated share of the One Maryland tax credits awarded by the Department of Business and Economic Development (DBED) in specified circumstances.

The bill takes effect July 1, 2012, and is applicable to all taxable years beginning after December 31, 2010. The altered definition of qualified distressed county terminates June 30, 2016.

Fiscal Summary

State Effect: Based on the historical average value of One Maryland tax credits awarded and the assumption that Baltimore City and Cecil, Dorchester, and Washington counties regain their designation as a distressed county in FY 2013, general fund revenues decrease by approximately $1 million in FY 2013. Transportation Trust Fund (TTF) revenues decrease by $65,300 in FY 2013 as a result of credits claimed against the corporate income tax and Higher Education Investment Fund (HEIF) revenues decrease by $48,600. Future revenue losses assume Baltimore City and Cecil, Dorchester, and Washington counties retain their designation through FY 2018, and DBED continues to certify projects at its 10-year average of $16.6 million annually. Special fund revenues may decrease in FY 2013 and annually thereafter due to decreased fees paid by businesses receiving financial assistance. General fund expenditures for the Comptroller's Office increase by $19,360 in FY 2013 for a one-time programming expense.

($ in millions)	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
GF Revenue	($.97)	($1.59)	($2.27)	($2.96)	($3.71)
SF Revenue	($.11)	($.32)	($.46)	($.60)	($.68)
GF Expenditure	$.02	$0	$0	$0	$0
Net Effect	($1.10)	($1.91)	($2.74)	($3.57)	($4.39)

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

Local Effect: Local highway user revenues decrease as a result of additional One Maryland credits being claimed against the corporate income tax. Expenditures in certain local jurisdictions receiving certain Maryland Economic Development Assistance Authority and Fund (MEDAAF) assistance and school construction funds may decrease as discussed below.

Small Business Effect: DBED advises that this bill has minimal or no impact on small business (attached). Legislative Services concurs with this assessment.

Analysis

Bill Summary: For any taxable year before the fifteenth taxable year after which a business entity may first take the One Maryland tax credit, the business entity may claim a prorated share of the credit for eligible project or start-up costs if the number of qualified positions filled by the business entity falls below 25, but does not fall below 10, and the business entity has maintained at least 25 qualified positions for at least 5 years. The prorated credit is calculated based on the number of qualified positions filled for the taxable year divided by 25. A business entity may also claim a prorated share of a tax refund for eligible project or start-up costs in any taxable year after the fourth but before the fifteenth taxable year following the year in which the business entity may first take the credit.

Current Law:

Qualified Distressed County

To qualify as a distressed county, a county must have:

- an average unemployment rate that must exceed 150% of the State's average during the preceding 24-month period; or
- a per capita personal income that may not exceed 67% of the State's average during the preceding 24-month period.

In addition to increasing, from 18 months to 24 months, the period by which a county's average unemployment rate is determined, Chapter 498 of 2008 provided an exception to the designation of a distressed county by specifying that a distressed county includes any county that no longer meets the unemployment and personal income criteria but has met at least one of the criteria at some point in the preceding 12-month period, which was subsequently extended to the preceding 24-month period by Chapter 891 of 2011.

DBED advises that the designation of a qualified distressed county impacts the One Maryland Tax Credit Program, MEDAAF, and the Maryland Industrial Financing Authority (MIDFA).

One Maryland Tax Credit Program

Businesses that establish or expand a business facility in a priority funding area (PFA), and are located in a qualified distressed county, may be entitled to tax credits for costs related to the new or expanded facility. The credit for start-up costs is the lesser of 100% of eligible start-up costs (up to $500,000), less any credits taken in prior years, or $10,000 multiplied by the number of employees that have filled the newly created, qualified positions.

The credit for project costs is the lesser of 100% of eligible project costs (up to $5 million), less any credits taken in prior years, or the State income tax liability for the taxable year from the project. Qualifying costs and expenses include those incurred with the acquisition, construction, rehabilitation, installation, and equipping of an eligible project. Eligible costs include land acquisition, performance and contract bonds, insurance, architectural and engineering services, environmental mitigation, and utility installation. The business must expend at least $500,000 in project costs.

Credits may be carried forward up to 14 successive tax years. The program specifies that the credits can be claimed against certain income and taxes in each year and provides for the refundability of the credit in certain circumstances. The program regulations require a business entity to maintain at least 25 qualified employees at the project to carry over a tax credit from the preceding year.

MEDAAF

MEDAAF provides below-market, fixed-rate financing in the form of loans, grants, conditional loans, conditional grants, and direct investment to local jurisdictions and businesses, particularly in growth industries and PFAs. MEDAAF provides businesses located in qualified distressed counties that qualify with enhanced financing terms and structuring. In addition, the amount of direct assistance provided to local jurisdictions is increased from a maximum of 70% to 100% of the project cost if the project is located in a qualified distressed county. In general, a local jurisdiction must provide a matching contribution equal to the amount of funding received under the Regional or Local

Revolving Fund. If the jurisdiction is located in a qualified distressed county, this matching amount is lowered to 50% of the State funds received.

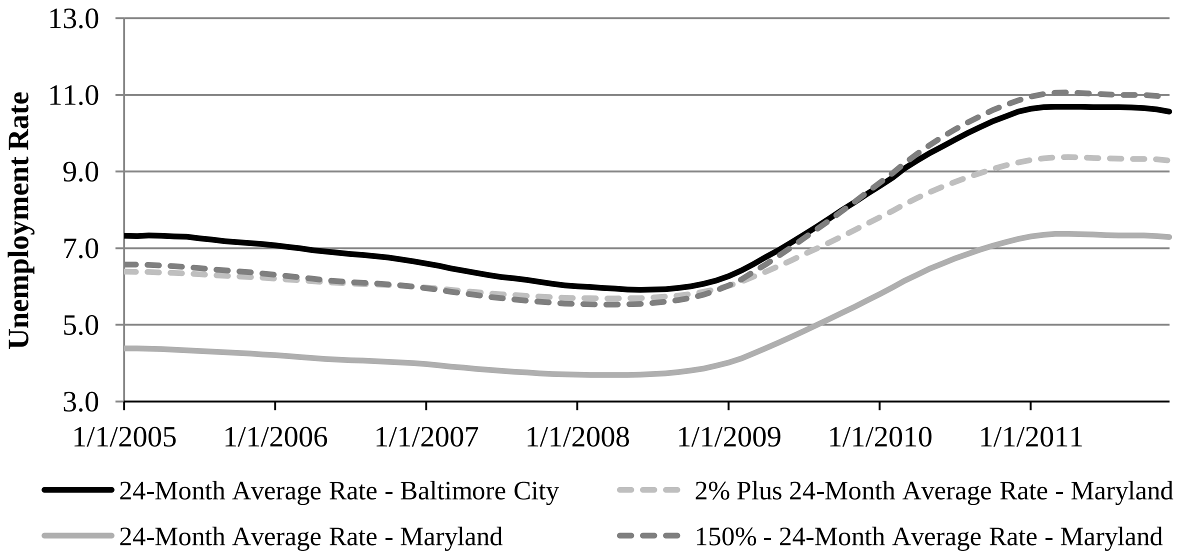
MIDFA

MIDFA was established by the General Assembly in 1965 to promote significant economic development by providing financing support to manufacturing, industrial, and technology businesses located in or moving to Maryland. MIDFA does not provide direct loans but insures bonds, loans, and certain other types of transactions from financial institutions. The program promotes private-sector financing by providing insurance to transactions resulting in reduced credit risks and enabling better terms. Recipients generally must pay bond issuance fees and annual premiums of one-half of 1% of all insured transactions, unless waived because the project is located in a qualified distressed county.

Background: DBED awarded $26.2 million in One Maryland tax credits in fiscal 2010 and $5.5 million in fiscal 2011. Since the program's inception, DBED has awarded credits to 44 projects that incurred a total of $165.7 million in project and start-up costs. A little more than two-thirds of all credits have been awarded to projects located in Baltimore City, followed by Cecil (9%), Garrett (5%), Allegany and Caroline (7% each), and Worcester and Dorchester counties (2% each).

As shown in **Appendix 1**, Allegany, Caroline, Somerset, and Worcester counties currently meet the criteria for designation as distressed counties. As of March 2010, Baltimore City did not meet either criteria, however, it remains eligible through March 2012 due to an extension of the eligibility grace period from 12 months to 24 months. **Exhibit 1** tracks the 24-month rolling average of the unemployment rate in Baltimore City. It also tracks the unemployment rate necessary to qualify as a distressed county under current law and under the bill. Relative county-level personal income is less volatile than county unemployment, with most counties tracking within a 5% range over the 2005 through 2009 period. The counties within range of the personal income threshold are Allegany, Caroline, Dorchester, and Somerset. However, only Allegany, Caroline, and Somerset currently qualify by the personal income threshold.

Exhibit 1
24-Month Average Unemployment Rate – Baltimore City and Maryland
Eligibility Level – Current Law vs. HB 1289



Source: U.S. Department of Labor, Bureau of Labor Statistics

Office of Legislative Audits – One Maryland Tax Credit

The Office of Legislative Audits in the Department of Legislative Services completed an audit of DBED in February 2012. The audit looked at the period beginning in October 2007 and ending in November 2010. The audit disclosed that DBED did not require applicants of the One Maryland program to submit supporting documentation for reported project and start-up costs on which the credit is based. On a test of 10 tax credit applicants totaling $42 million, eight applicants certified for $34 million in credits did not provide any documentation of the costs. Of the eight applicants who did not submit documentation, four took One Maryland tax credits totaling $11.7 million from calendar 2006 through 2009. The audit recommended that DBED obtain adequate supporting documentation for project and start-up costs prior to certifying applicants. DBED agreed with the auditor's recommendation and agreed to immediately amend the preliminary and final tax credit applications to include an accounting for start-up and project costs.

State Fiscal Effect: Based on the assumption that Baltimore City and Cecil, Dorchester, and Washington counties would otherwise not be designated as qualified distressed counties, and that DBED continues to certify projects at its 10-year average of

$16.6 million annually, general fund revenues decrease by $965,700 in fiscal 2013. In addition, TTF revenues decrease by $65,300 and HEIF revenues decrease by $48,600 in fiscal 2013. Out-year revenue decreases reflect DBED certifying additional projects at its 10-year average, and that Baltimore City and Cecil, Dorchester, and Washington counties meet the bill's unemployment eligibility criteria through the provision's termination date in fiscal 2016, and thus retain their designation as qualified distressed counties through fiscal 2018 due to the 24-month eligibility grace period. All revenue decreases assume qualifying businesses amortize the entire certified start-up or project costs over 15 years.

The bill allows specified businesses to continue to claim the tax credit on a prorated basis if the number of qualified positions filled by the business falls below 25, but remains above 10. Revenue decreases reflect three businesses each year claiming a prorated credit for 20 employees, based on the average annual wage of employees in the program of $54,000.

Special fund revenues may decrease at DBED in fiscal 2013 and annually thereafter due to a decreased amount of fees paid under MIDFA for projects located in qualified distressed counties. Any impact is not expected to be significant. The bill does not impact the overall funding provided under MEDAAF or MIDFA. General fund expenditures increase for the Comptroller's Office by $19,360 in fiscal 2013 for a one-time programming expense to reconfigure the tax credit instructions and form to the bill.

There is no fiscal impact due to changing the definition of qualified distressed county as it applies to the College Readiness Outreach Program or the Linked Deposit Program.

Local Fiscal Effect: Local governments receive a portion of TTF revenues as local highway user revenues for the purpose of constructing and maintaining local roads. Pursuant to this legislation, local highway user revenues decrease by $6,300 in fiscal 2013 and additionally in out-years.

To the extent certain counties gain designation as a qualified distressed county, expenditures may decrease in local jurisdictions located in these counties due to a decrease in the amount of matching grant payments required for projects receiving funding under MEDAAF's regional or local revolving loan funds or direct assistance to local jurisdictions' programs.

The bill does not impact the total amount of local revenues from State school construction aid, but the distribution of that aid among local school systems may change. The impact on the amount of local expenditures required to match State school construction aid if any, will not occur until fiscal 2016 when the State and local cost-sharing formula is recalculated. The formula provides a higher State share for qualified distressed counties.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Department of Business and Economic Development; Department of Budget and Management; Department of Housing and Community Development; Maryland Insurance Administration; Comptroller's Office; Department of Labor, Licensing, and Regulation; U.S. Department of Labor; Department of Legislative Services

Fiscal Note History:	First Reader - March 8, 2012
ncs/rhh	Revised - Updated Information - March 9, 2012

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Appendix 1

County	24-month Average Unemployment Rate (Dec. 2011)	% of 24-month Average Unemployment Rate (Dec. 2011)	% of 24-month Average of State per Capita Personal Income (Dec. 2011)	Qualified – Current Law: Unemployment Rate	Qualified – Current Law: Per Capita Personal Income	Qualified – HB 1289: Unemployment Rate	Qualified – HB 1289: Per Capita Personal Income
Allegany	8.9	124%	65%	-	Yes	-	Yes
Anne Arundel	6.6	92%	113%	-	-	-	-
Baltimore City	10.6	147%	104%	Yes*	-	Yes	-
Baltimore	7.8	108%	77%	-	-	-	-
Calvert	6.0	83%	90%	-	-	-	-
Caroline	9.1	126%	63%	-	Yes	-	Yes
Carroll	6.5	90%	88%	-	-	-	-
Cecil	9.4	131%	77%	-	-	Yes	-
Charles	6.1	85%	88%	-	-	-	-
Dorchester	10.5	146%	69%	-	-	Yes	-
Frederick	6.3	88%	93%	-	-	-	-
Garrett	7.7	107%	72%	Yes**	-	-	-
Harford	7.3	101%	95%	-	-	-	-
Howard	5.3	74%	129%	-	-	-	-
Kent	8	111%	93%	-	-	-	-
Montgomery	5.4	75%	139%	-	-	-	-
Prince George's	7.2	100%	82%	-	-	-	-
Queen Anne's	6.9	96%	95%	-	-	-	-
Somerset	10	139%	56%	-	Yes	Yes	Yes
St. Mary's	6.1	85%	85%	-	-	-	-
Talbot	7.6	106%	119%	-	-	-	-
Washington	9.9	138%	72%	-	-	Yes	-
Wicomico	8.7	121%	72%	-	-	-	-
Worcester	12.4	172%	86%	Yes	-	Yes	-
Maryland	**7.2**	**-**	**$48,360**				

*Through March 2012
** Through April 2012

Source: U.S. Bureau of Labor Statistics

ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES (SFY 2012)

TITLE OF BILL: Business and Economic Development – Qualified Distressed Counties

BILL NUMBER: N.A.

PREPARED BY: Alfredo B. Goyburu (Department of Business and Economic Development, Office of Marketing and Communications)

PART A. ECONOMIC IMPACT RATING

This agency estimates that the proposed bill:

XX WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND SMALL BUSINESS

OR

WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND SMALL BUSINESSES

PART B. ECONOMIC IMPACT ANALYSIS

The current definition of a ―qualified distressed county‖ (QDC), threatens the QDC status for Baltimore City and Garrett County. This bill would expand the definition of a QDC in a manner that would restore QDC status to jurisdictions that have historically qualified as ―distressed‖. Under the proposal a county or Baltimore City could qualify as a QDC if, over the previous two years, its unemployment rate averaged at least 2.0 percentage points higher than the State unemployment rate over the same period. So a county qualifying under the current law definition or under the proposed criterion could qualify as a QDC. In addition to restoring Baltimore City to QDC status, the proposal would add Washington and Cecil counties.
This bill also prorates the Tax Credit in situations where businesses may not be able, due to the economic climate, to maintain the number of jobs for which they were originally certified. At present, if a qualified business entity cannot claim the entire credit in one year (because the amount of the credit exceeds their State tax liability), the qualified business entity may claim the excess funds for up to fourteen (14) years (not including the year the project becomes eligible). This legislation would permit a qualified business entity to claim a portion of the tax credit, within the fifteen (15) years, even if they fell below the required number of jobs. Specifically, qualified business entities will be able to claim a prorated share of the tax credit even if after 5 years the number of qualified positions falls below twenty-five (25). The business entities will however, have to maintain at least ten (10) qualified positions. The prorated share of the credit will be calculated based on the number of qualified positions filled for the taxable year divided by twenty-five (25).

QDC status affects a jurisdiction's participation in the One Maryland tax credit program and the One Maryland MEDAAF funding program. To assess the effect of the proposed change on

Maryland-based small business, one should examine how these programs have affected small business in the recent past.

To evaluate the effects of the One Maryland tax credit, we define a small business as a Maryland-based firm with 99 or fewer employees. During SFY 2001 to SFY 2011, 44 One Maryland tax credit final certifications were issued. Our research found seven certifications were issued to Maryland small businesses, including two to the same firm. In addition nine were issued to establishments employing 99 or fewer employees in Maryland, but part of a larger firm. We did not regard the latter group of firms as small businesses.

During SFY 2005 to SFY 2010, 35 projects have been approved under One Maryland MEDAAF. Of these, one of these projects had its approval rescinded and five were associated with Maryland small businesses. This indicates that the One Maryland MEDAAF program has directly affected five small businesses over six years.

The modest total of six different small firms affected by the One Maryland tax credits, over the eleven-year period, indicates this change would exert a minimal economic impact on Maryland small business. This finding is further supported by the modest rate of small business direct involvement in One Maryland MEDAAF—five small firms over six years.