HB 1181

Department of Legislative Services

Maryland General Assembly
2017 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1181 (Delegate B. Wilson)
Ways and Means

Economic Development - Municipal Corporations - Community Revitalization and Improvement Zones

This bill establishes State tax benefits for eligible municipalities with qualified businesses located in community revitalization and improvement zones. A municipality may issue bonds pledging specified income and sales tax revenues from businesses located or partially located in a zone. The bonds may only be used for (1) development or improvement within a zone and (2) specified types of construction. After the amount of eligible taxes paid by qualified businesses in each zone is certified, the Comptroller must transfer State general funds to each municipality's special fund, as provided in the State budget, to be used only for debt service on the bonds or for other specified related purposes. State payments to municipalities continue until retirement of the bonds or debt and for no more than 20 years.

Fiscal Summary

State Effect: General fund expenditures increase significantly, beginning as early as FY 2019, to the extent that eligible municipalities pledge State tax revenues to improvements in zones; the amount cannot be reliably estimated at this time. General and special fund revenues increase to the extent that the bill leads to additional economic development. General fund expenditures for the Department of Housing and Community Development (DHCD) increase by $125,300 in FY 2018 for staff and related expenses. Future year expenditures reflect annualization and the elimination of one-time costs. The Comptroller can likely implement the bill with existing budgeted resources.

(in dollars)	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
GF Revenue	$0	-	-	-	-
SF Revenue	$0	-	-	-	-
GF Expenditure	$125,300	$157,700	$164,900	$172,400	$180,300
Net Effect	($125,300)	(-)	(-)	(-)	(-)

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

Local Effect: Local government revenues increase from bonds issued under the bill beginning as soon as FY 2018, with State payments beginning in FY 2019 for up to 20 years. Local government expenditures increase correspondingly for authorized purposes within community revitalization and improvement zones. Local income tax revenues increase to the extent that the bill leads to additional economic development; however, the revenues dedicated to the special fund are unavailable for other uses. Local property tax revenues increase to the extent that the expenditures increase property values.

Small Business Effect: Meaningful.

Analysis

Bill Summary: "Eligible tax" means (1) the corporate income tax and personal income tax, including the county income tax, to the extent the tax is related to an activity of a qualified business within a community revitalization and improvement zone or work performed by an employee of a qualified business within a zone and (2) the sales and use tax to the extent the tax is related to an activity of a qualified business within a zone.

"Qualified business" means an entity located or partially located in a community revitalization and improvement zone that (1) conducts an active trade or business in the zone and (2) appears on the list of qualified entities required to be filed under the bill. A qualified business is also a business that moves into the zone after the zone is established, conducts an active trade or business in the zone, and is added to the list of qualified entities. It includes a contractor engaged in construction (including infrastructure or site preparation), reconstruction, or renovation of a facility located in or partially located in a community revitalization and improvement zone. It does not include an agent, a broker, a representative of a business, or an entity that closes its business elsewhere in the State in conjunction with the move into a zone.

Community Revitalization and Improvement Zones

The governing body of a municipality that DHCD determines has experienced economic decline *may* establish, by local law, a contracting authority for the purpose of designating a community revitalization and improvement zone. A contracting authority *may* apply to DHCD for approval of a community revitalization and improvement zone plan. The application must include:

- an economic development plan to establish one or more facilities that will promote economic development;
- specific information relating to the facility or facilities that are affected by the plan;

- a description and map of the specific geographic area of the zone; and
- any other information required by DHCD.

The application must be approved by DHCD and the governing body of the municipality in which the zone is to be located. However, if an application is not disapproved by either DHCD or the governing body of the municipality within 90 days, the application is deemed to be approved.

Tax Increment Financing

A governing body of a municipality that establishes a contracting authority must establish a special fund that may only be used for debt service and other specified related purposes, including reasonable administrative costs of the contracting authority. A member of the contracting authority may not receive money directly or indirectly from the special fund.

On approval of an application, a contracting authority may (1) designate a community revitalization and improvement zone where a facility may be constructed, reconstructed, or renovated and (2) apply to the municipality to issue bonds pledging revenue transferred to a special fund established by the municipality. The governing body of the municipality may then issue bonds pledging revenue transferred to the special fund for specified uses within a zone that will result in economic development in accordance with the contracting authority's plan.

"Baseline year" means the calendar year in which a community revitalization and improvement zone is established. By June 1 following the baseline year and annually thereafter, each contracting authority must file with DHCD a list of (1) all businesses located in the zone and (2) all contractors engaged in construction, reconstruction, or renovation of a facility in the zone. The list must include, for each business, the address, State tax identification number, and location within the zone. If the list is not provided to DHCD in a timely manner, DHCD may not certify any eligible tax for the prior calendar year.

By June 1 following the baseline year and annually thereafter, each qualified business must file a report with DHCD that includes (1) the amount of each eligible tax that was paid to the State by the business in the prior calendar year and (2) the amount of eligible tax refund received from the State by the business in the prior calendar year.

By October 15 following the baseline year and annually thereafter, DHCD must verify the baseline year tax amount, which consists of the amount of eligible tax paid during the baseline year, less eligible tax refunds. The bill specifies requirements for a qualified business that is not included in the baseline tax year amount – because it moves into the zone, after the baseline year, from within the State or is in the zone but is not included in the calculation of the baseline tax amount. Generally, the eligible taxes are added to the baseline tax amount. This requirement does not apply to a qualifying business that moves into a zone from outside the State.

By October 15 of the year following the baseline year and annually thereafter, DHCD must make the following calculation for qualified businesses (separately for each zone) by:

- subtracting the amount of eligible tax refunds received from the State from the amount of eligible tax paid to the State; and
- subtracting the baseline tax amount for the community revitalization and improvement zone from the above amount.

DHCD must then certify this amount to the Comptroller. The certification may include (1) an adjustment made to timely filed reports with DHCD for eligible tax actually paid by a qualified business in the prior calendar year and (2) eligible tax refunds paid to a qualified business in the community revitalization and improvement zone in the prior calendar year. The certification may *not* include tax paid by a qualified business (1) that did not file a timely report or (2) if the tax was not included in the State baseline year tax amount.

Within 10 days after receiving the certification from DHCD, the Comptroller must transfer from the State general fund, as provided in the State budget, the amount of certified eligible tax to each municipal special fund established under the bill.

A community revitalization and improvement zone must be in effect for a period equal to the length of time necessary for repayment of the bonds issued or debt incurred on behalf of the zone. Bonds must be retired and all community revitalization and improvement zones must be dissolved no later than 20 years following the initial issuance of the bonds.

The amount transferred to the special fund must first be used to pay debt service on any outstanding bonds. It may then be used for other specified related purposes, including construction, improvement projects, replenishment of debt service reserve funds, and reasonable administrative costs of the contracting authority. The transfer of money from the special fund utilized for new construction, reconstruction, or renovation of facilities is subject to a match of private funds at a ratio of 5 fund dollars to 1 private dollar. The transfer of money from the special fund utilized for renovation or rehabilitation of qualified historic structures and facilities is subject to a match of private funds at a ratio of 10 fund dollars to 1 private dollar.

If the amount of money transferred to the special fund in any one calendar year exceeds the money utilized in that calendar year, the contracting authority must return the excess money to the Comptroller by January 15 of the following year for deposit into the general fund.

The contracting authority must file an annual report with DHCD by April 1 of each year following the baseline year, which must contain a detailed account of fund expenditures and a calculation of the match ratios.

Other Provisions

DHCD, in consultation with the Comptroller, must adopt regulations to implement the bill.

A portion of a community revitalization and improvement zone in which a facility has not been constructed, reconstructed, or renovated using funds under the bill may be transferred out of the zone and additional acreage may be added to the zone, subject to DHCD approval.

Current Law: All counties and municipalities are authorized to utilize tax increment financing (TIF) under Title 12, Subtitle 2 of the Economic Development Article (the Tax Increment Financing Act). In Baltimore City, the authority to use TIF is provided in the city charter. Different geographic areas are eligible for TIF under various State programs. The "original base" for a TIF district means the assessable base of the district:

- as of January 1 of the year preceding the effective date of the resolution creating the district; or
- if applicable, the original base for a brownfields site as determined by resolution of the political subdivision.

Background: The bill establishes a similar structure to that in current law for TIF, except that incremental income and sales tax revenues are pledged to debt service payments rather than incremental property tax revenues.

TIF is a public financing method that uses future gains in *property* tax revenues to finance current improvements. The increase in the property tax revenue generated by new commercial development in a specific area, the TIF district, pays for bonds issued to finance site improvements, infrastructure, and other project costs located on public property. In a TIF district, the local government "freezes" the existing property tax base and uses the property tax revenue from this base as it would normally use such funds. The difference between the current tax base and the frozen base in each future year is termed the incremental valuation. The local government apportions the property tax revenue on the incremental valuation to a special account for certain purposes, including to pay debt service on the bonds and to potentially pay for additional public expenditures in the TIF district. The TIF district ceases to exist upon the retirement of the bonds, and after that time, all property tax revenue may be appropriated by normal means.

State Fiscal Effect: General fund expenditures increase significantly beginning as soon as fiscal 2019 and continue for up to 20 years for each zone to the extent that eligible municipalities establish community revitalization and improvement zones and pledge State and local tax revenues to debt service on bonds issued or for the purposes for which bonds may be used under the bill. The amount cannot be reliably estimated at this time, but it is anticipated to be significant because the bill pledges future State tax revenues to repay debt service on bonds issued by municipalities or funds used for those purposes. This is likely an attractive financing method for municipalities that have experienced economic decline and, therefore, would be used often.

Special fund revenues for the Annuity Bond Fund increase to the extent that the expenditures by local governments on infrastructure and construction increase property values. General and special fund revenues also increase to the extent the spending increases overall economic growth. These amounts cannot be reliably estimated at this time.

The bill creates additional administrative requirements for DHCD that are not absorbable within existing resources. Therefore, general fund expenditures increase by $125,347 in fiscal 2018, which accounts for the bill's October 1, 2017 effective date. This estimate reflects the cost of DHCD hiring two staff to oversee the program and its administrative tasks.

New Positions	2
Salaries and Fringe Benefits	$115,129
Other Operating Expenses	10,218
Total FY 2018 State Expenditures	**$125,347**

Future year expenditures reflect full salaries with annual increases and employee turnover and ongoing operating expenses.

The Comptroller can likely implement the bill with existing budgeted resources.

Local Fiscal Effect: Local government revenues increase from bonds issued under the bill as soon as fiscal 2018, with State payments beginning in fiscal 2019 for up to 20 years. Local government expenditures increase correspondingly for authorized purposes within community revitalization and improvement zones. Local income tax revenues increase to the extent that the bill leads to additional economic development; however, the revenues dedicated to the special fund are unavailable for other uses. Local property tax revenues increase to the extent that the expenditures increase property values.

Small Business Effect: Small businesses in community revitalization and improvement zones benefit from additional spending by municipalities on infrastructure and construction; however, they are also burdened with an annual reporting requirement. Small businesses that provide construction and related services benefit from additional demand for their services.

Additional Comments: The bill authorizes a municipality that has experienced economic decline to issue bonds with State revenues pledged to their repayment. The Department of Legislative Services advises that the bonds will almost certainly be construed as State debt by bond rating agencies and bondholders.

The Comptroller advises that the bill raises a number of implementation questions, including the fact that, without a substantial audit, DHCD or the Comptroller would not be able to verify the amount of certified eligible tax. Currently, businesses have no reason to differentiate revenues originating from different business locations in the State. For businesses that operate locations both inside and outside a zone, there are no mechanisms to apportion the tax revenues from activity that occurs in each location. The problem is further complicated if a single employee earns a salary while working at locations both inside and outside a zone.

Additional Information

Prior Introductions: Similar bills, HB 278 of 2016 and HB 916 of 2015, received hearings in the House Ways and Means Committee, but no further action was taken. A cross file, SB 415 of 2016, received a hearing in the Senate Budget and Taxation Committee, but no further action was taken.

Cross File: None.

Information Source(s): City of Bowie; Maryland Municipal League; Comptroller's Office; Department of Housing and Community Development; Department of Legislative Services

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