

SENATE BILL REPORT

E3SHB 1324

As Reported by Senate Committee On:
Financial Institutions, Economic Development & Trade, March 28, 2019

Title: An act relating to creating the Washington rural development and opportunity zone act.

Brief Description: Creating the Washington rural development and opportunity zone act.

Sponsors: House Committee on Appropriations (originally sponsored by Representatives Chapman, Maycumber, Springer, Chandler, Blake, Stokesbary, Steele, Reeves, Pettigrew, Dolan, Volz, Barkis, Eslick, Lekanoff, Tharinger, Hoff, Jinkins, Kilduff and Leavitt).

Brief History: Passed House: 3/07/19, 97-0.

Committee Activity: Financial Institutions, Economic Development & Trade: 3/19/19, 3/28/19 [DPA, DNP].

Brief Summary of Amended Bill

- Extends a reduced B&O tax rate and surcharge on certain activities related to the timber industry.
- Directs the Washington State Institute for Public Policy to conduct a study on certain programs incentivizing private investment and job creation in rural and distressed communities.

SENATE COMMITTEE ON FINANCIAL INSTITUTIONS, ECONOMIC DEVELOPMENT & TRADE

Majority Report: Do pass as amended.

Signed by Senators Mullet, Chair; Braun, Das, Ericksen and Hobbs.

Minority Report: Do not pass.

Signed by Senator Hasegawa, Vice Chair.

Staff: Kellee Gunn (786-7429)

Background: Rural and Small Business Investment Companies. Rural Business Investment Companies (RBIC) and Small Business Investment Companies (SBIC) are privately owned and managed investment funds, licensed and regulated by the United States Department of

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Agriculture (USDA) and the Small Business Administration (SBA), respectively. Both allow for capital investments in small businesses and smaller enterprises located in rural areas. Both RBICs and SBICs raise private capital from investors and may receive borrowed capital from the USDA or SBA, respectively, in order to fund the investments.

An RBIC or SBIC program is a provision in a state or federal tax code that offers incentives for private capital to invest in small businesses, startups, low-income areas, or regions otherwise under economic distress. These programs often include special criteria for a certain quantity of the credit to focus on rural or underdeveloped areas.

Incentivizing Private Investment and Job Creation in Rural Areas. Since the 1980s, certain programs have been developed and enacted in states to incentivize private investment and job creation in rural areas. These programs began as Certified Capital Company Programs (CAPCOs), then became New Markets Tax Credit Programs (NMTCs), and are now referred to as Rural Jobs Programs. These programs include similar elements to each other including providing certain companies, such as SBICs or RBICs, tax credits in exchange for investing in rural areas.

Business and Occupation Tax Rate on Timber Activities. On July 1, 2007, the B&O tax rate was reduced to 0.003424 for certain activities related to the timber industry including:

- standing timber sales;
- extracting or extracting for hire timber;
- manufacturing or processing for hire timber into timber, wood, or other products; and
- selling certain timber and wood products at wholesale.

The preferential rate is comprised of a base rate of 0.2904 percent plus a surcharge of 0.052 percent. This reduced B&O tax rate will expire June 30, 2024.

Summary of Amended Bill: Study on Certain Statewide Economic Development Programs for Rural and Distressed Communities. The Washington State Institute for Public Policy (WSIPP) is directed to conduct a study on certain programs incentivizing private investment and job creation in rural and distressed communities. In conducting the study, WSIPP must:

- conduct a 50-state review on the structure and characteristics of CAPCOs, NMTCs, rural jobs programs, and other similar economic development programs in other states; and
- review any available research on these initiatives and, to the extent possible, describe the effects of each type of initiative on employment, earnings, property values, and job creation.

The report is due to the appropriate committees of the Legislature by July 1, 2020.

Timber B&O Tax and Surcharge Certain Wood Products. The reduced B&O tax rate on certain activities related to the timber industry is changed from July 1, 2024, to July 1, 2036. The expiration for a surcharge imposed on certain timber and wood product manufacturers, extractors, and wholesalers is changed from July 1, 2024, to July 1, 2036. The extension of the reduced tax rate is exempted from the requirement to include a tax preference performance statement.

EFFECT OF FINANCIAL INSTITUTIONS, ECONOMIC DEVELOPMENT & TRADE COMMITTEE AMENDMENT(S):

- Directs the Washington State Institute for Public Policy to conduct a study on certain programs incentivizing private investment and job creation in rural and distressed communities.
- Removes language creating the Rural Development and Distressed Opportunity Zone Program.

Appropriation: The bill contains a null and void clause requiring specific funding be provided in an omnibus appropriation act.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony on Engrossed Third Substitute House Bill: *The committee recommended a different version of the bill than what was heard.* PRO: This bill passed off the House floor unanimously. My legislative district has high unemployment, and these rural areas have a difficulty raising capital. This is an opportunity to put \$100 million in the most rural and distressed areas of the state. There is no risk to the state, and this legislation has claw back provisions if it does not perform. This revenue is not part of our budget outlook right now. Programs like this one have been around for decades; they began as CAPCO programs, then New Markets Tax Credit programs, and are now rural jobs programs. If we had dynamic fiscal notes, this legislation would not have a cost.

This has the strongest claw back provisions of any other program in the United States. These companies have skin in the game, and are required to have a 10 percent ownership. Through the program in Wyoming, jobs were created and there was access to capital that did not exist before. After some time, the Wyoming businesses were able to shift back to banks for funding. This has potential to bring investment into rural companies and lead to job growth. Section 9 of this bill incorporates claw back provisions to recapture investment. The state is investing in these businesses, and you want the requirements of these investment companies to be strong.

Back in 2006, the timber industry was looking for parity with the aerospace industry and a preferential B&O tax rate was created. The surcharge is used to fund participation grants. The preferential B&O tax rate, and the surcharge, should continue.

CON: This is an ineffective program. Over the recent legislative cycles, many states have passed bills like this one. These investment firms adjust the programs for whatever state legislators are willing to pass. The way this bill is written, only a few companies may take advantage of this program. No Washington-based firms would be eligible because none of them are federal RBICs or SBICs and being in one of those programs is a criterion for certification.

Recipients of these funds may not even be in Washington State as the legislation does not require a targeted small business, which is eligible to receive funding, to maintain its status during the entire time that the fund maintains its investment in that business. We agree with the intent of this bill, but this approach is fundamentally flawed. This is designed to support certain firms with bad track records of creating jobs. State auditors in states with programs like this have suggested to close the programs. This is not the Office of Financial Management who will be doing the economic analysis, but a private firm hired by the investment firms.

The extension of the timber tax will cost \$135 million to the state. The state could use the \$60 million in tax credits in the Rural Development and Distressed Opportunity Zone Act and instead invest it in Community and Technical Colleges, which would have a multiplier effect and would benefit at least 10,000 students.

OTHER: There is a mixed track record of these programs in other states. Considering the tax preference, what is the expectation of the jobs created per the state's investment? There is a need for small business loans, at low interest. When you think of opportunities to work on economic development, there are other options for investment including broadband or other infrastructure projects. There is a need for investment in rural areas.

We are in support of extending the preferential B&O tax rate for forest products and the surcharge on timber manufacturers that funds the adaptive management program at the Department of Natural Resources (DNR). The cap on the surcharge should be removed and revert to the language that was in previous versions that had been agreed to by the tribes, DNR, and the timber industry. Extending the surcharge will ensure the important work being done by the adaptive management program at DNR continues. The B&O reduction was originally tied with the surcharge, and they need to go forward together. The \$8 million cap on the surcharge in Section 16 should be lifted to provide more funding for the adaptive management program and other grants. The federal funding provision should also be lifted. By lifting the federal funding condition, it would save the state money as there is still a requirement for the state to provide funding to the tribes for this purpose.

Persons Testifying: PRO: Representative Mike Chapman, Prime Sponsor; Trent House, Washington Bankers Association; Mike Ennis, Association of Washington Business; Steve Gano, Advantage Capital; Jennifer Ziegler, Washington Economic Development Association; Bill Stauffacher, Enhanced Capital; John Ehrenreich, Washington Forest Protection Association; Daryl Williams, Tulalips Tribes.

CON: Andy Nicholas, Washington State Budget and Policy Center; John Burbank, Economic Opportunity Institute; Erin Haick, SEIU 925; Darrell Johnson, citizen; Julia Sass-Rubin, Rutgers University.

OTHER: Jasmine Vasavada, Department of Commerce; Joanna Eide, Department of Natural Resources; Jim Peters, Northwest Indian Fisheries Commission.

Persons Signed In To Testify But Not Testifying: No one.