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FISCAL IMPACT STATEMENT

LS 7008 | **NOTE PREPARED:** Jan 17, 2006
BILL NUMBER: HB 1393 | **BILL AMENDED:**

SUBJECT: Community Development Financial Institutions.

FIRST AUTHOR: Rep. Reske | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X GENERAL | **IMPACT:** State & Local
X DEDICATED
FEDERAL

Summary of Legislation: The bill requires the Economic Development Corporation (IEDC) to implement a program to provide financial and technical assistance to: (1) federally certified community development financial institutions (CDFI); (2) Indiana CDFIs; and (3) Local CDFIs; that make loans and investments or provide services to targeted investment areas or to targeted low-income populations. It authorizes the IEDC to designate entities meeting certain requirements as Indiana CDFIs and to designate counties and municipalities (or foundations established by a county or municipality) meeting certain requirements as Local CDFIs. It also allows the IEDC to provide grants, loans, and technical assistance to a CDFI, an Indiana CDFI, or a Local CDFI for certain purposes related to remedying a lack of adequate access to loans, equity investments, mortgage lending, banking services, or personal financial services of a targeted low-income population or in a targeted investment area.

The bill specifies the criteria to be used by the IEDC in determining whether to award a grant or loan or provide technical assistance. It requires the IEDC to serve as a clearinghouse for information relevant to potential incorporators or organizers of CDFIs, Indiana CDFIs, and Local CDFIs. It provides that the IEDC may not provide any combination of grants or loans under the program to a single entity that exceeds the greater of 10% of the total assets of the Community Development Financial Institutions Fund or $500,000.

The bill authorizes CDFIs, Indiana CDFIs, and Local CDFIs to apply for a loan or grant from the Microenterprise Partnership Program Fund (fund), and authorizes those entities to establish local investment pools and local opportunity pools under the Microenterprise Partnership Program. The bill specifies that grants may be made from the Fund.

The bill encourages the Public Employees' Retirement Fund (PERF) Board and the Teachers' Retirement Fund (TRF) Board to establish a goal for investment in funds that invest in CDFIs and Indiana CDFIs. The bill provides that the PERF Board and the TRF Board are not required to achieve the goals if the Boards, exercising financial and fiduciary prudence, determine that sufficient appropriate investments in CDFIs and Indiana CDFIs are not available in Indiana.

The bill establishes the State New Markets Tax Credit for a taxpayer that qualifies for the federal New Markets Tax Credit administered by the federal Community Development Financial Institutions Fund. It also provides that the amount of tax credits allowed may not exceed $5,000,000 in a state fiscal year.

Effective Date: January 1, 2006 (retroactive); July 1, 2006.

Explanation of State Expenditures: *CDFI Assistance Program:* The bill requires the IEDC to implement a program to provide financial and technical assistance to federally designated Community Development Financial Institutions, Indiana CDFIs, and Local CDFIs. The bill defines a CDFI as an entity designated as such by the U.S. Department of Treasury's Community Development Financial Institutions Fund. The bill also allows the IEDC to designate Indiana CDFIs and Local CDFIs that are not federally designated but perform activities consistent with the federal CDFI program. The bill requires the financial and technical assistance program to include federally designated CDFIs, Indiana CDFIs and Local CDFIs. The bill specifies criteria that must be met by a CDFI to receive financial assistance (loans and grants), and requires the CDFI to enter into a financial assistance agreement with the IEDC. The bill creates the CDFI Fund to be administered by the IEDC. Financial assistance to CDFIs would be provided from this Fund. The Fund is non-reverting. The bill does not appropriate money to the CDFI Fund.

Background: The bill authorizes the IEDC to make loans as the sole lender or in cooperation with other lenders. The bill limits any combination of grants or loans to an entity to the greater of: (1) 10% of the total assets of the Fund; or (2) $500,000. The bill provides that loans, grants, and technical assistance may be used:

(1) In the case of a CDFI or Indiana CDFI, for the provision of basic financial services, the development of loan products, or the provision of below-market-rate financing in targeted investment areas and to low-income persons.

(2) For the development of commercial facilities that promote revitalization, community stability, and the creation or retention of jobs.

(3) For training of management and other personnel.

(4) For housing that is affordable to low-income persons, except that assistance used to facilitate home ownership shall only be used for services and loans that: (a) serve low-income persons; and (b) are not sufficiently provided by other lenders in the area or complement the services and loans provided by other lenders in the area.

(5) To provide financial assistance to businesses that: (a) provide jobs for low-income persons or are owned by low-income persons, women, or minority entrepreneurs; (b) enhance the availability of products and services to low-income persons; or (c) have loan requests of not more than $25,000 and have not more than 5 employees.

(6) In the case of an Indiana CDFI, to obtain federal certification as a CDFI.

(7) For other activities approved by the IEDC.

There are more than 1,000 CDFIs designated by the U.S. Treasury Department's CDFI Fund operating in the U.S., with 7 operating in Indiana. The primary mission of federally designated CDFIs is to promote economic development in struggling areas, both urban and rural, that are underserved by traditional financial institutions. Annually, the federal government provides financial assistance to CDFIs in the form of equity investments, loans, deposits, or grants. The financial assistance must be matched, dollar for dollar, by the CDFI with non-federal source funds. The CDFIs provide various financial services to their target areas, including mortgage financing for home buyers, financing for the rehabilitation of rental housing, financing for the building and rehabilitation of community facilities, commercial loans to small and microenterprise businesses, and financial services needed by low-income households and businesses in the target areas.

The bill authorizes the IEDC to designate (1) a for-profit or nonprofit entity as an Indiana CDFI; or (2) a county or municipality, or a nonprofit foundation established by a county or municipality, as a Local CDFI if it meets the following conditions:

(1) The entity is located in Indiana or is doing business or providing services in Indiana.

(2) The entity: (a) has as a purpose the promotion of community development; (b) provides loans, investments, banking services, or development services in a targeted investment area or to a targeted population; or (c) is considered by the corporation to perform activities consistent with the goals of the federal CDFI program.

In the case of an Indiana CDFI, the entity can not be a Local CDFI or a CDFI designated by the U.S. Department of the Treasury's CDFI Fund.

As part of the CDFI Program, the bill requires CDFIs that receives grants, loans, or technical assistance from the IEDC to annually report including: (1) the total amount of capital raised by the CDFI; (2) the total amount of capital invested or loaned in targeted investment areas or to targeted populations; (3) the amounts and types of jobs created or retained by the investment or loans; (4) a summary of the CDFI's activities during the year; and (5) any other information required by the IEDC. Targeted areas include Enterprise Zones; federal Empowerment Zones or Enterprise Communities; economically distressed areas; or areas with significant unmet financial services needs. Targeted populations include low-income persons or persons lacking adequate access to financial services. The bill also requires the IEDC to annually report to the Governor and the General Assembly information regarding: (1) the applications for assistance filed and approved by the IEDC; (2) the amount and type of assistance provided; (3) a description of projects financed or assisted by grants or loans; (4) an estimate of the number of jobs created or retained through the grants and loans; and (5) the amount and source of other money leveraged or matched by grants or loans. The IEDC's current level of resources should be sufficient to fulfill these administrative tasks. The December 5, 2005, state staffing table indicates that the IEDC had 39 vacant full-time positions, including one regional office position.

Microenterprise Programs: The bill allows the IEDC to provide loans and grants from the Microenterprise Partnership Fund to federally designated CDFIs, Indiana CDFIs, and Local CDFIs. Currently, the IEDC may use money in the Fund to provide loans under the Small Business Development Program; loans and loan guarantees under the Small and Minority Business Financial Assistance Program; and to carry out the Microenterprise Partnership Program. The bill also specifies that federally designated CDFIs, Indiana CDFIs, and Local CDFIs are microloan delivery organizations for purposes of the Microenterprise Partnership Program.

State New Markets Tax Credit (NMTC): The bill requires the Indiana Economic Development Corporation to establish a program for certifying State NMTCs. The IEDC's current level of resources should be sufficient to fulfill these administrative tasks. The December 5, 2005, state staffing table indicates that the IEDC had 39 vacant full-time positions, including one regional office position.

Department of State Revenue (DOR): The DOR will incur additional expenses to revise tax forms, instructions, and computer programs to reflect the new State New Markets Tax Credit. The Department's current level of resources should be sufficient to implement this change.

Explanation of State Revenues: *State New Markets Tax Credit:* This bill establishes the State New Markets Tax Credit for taxpayers that qualify for the federal NMTC. The credit may be taken against the taxpayer's Adjusted Gross Income (AGI) Tax liability, Financial Institutions Tax liability, or Insurance Premiums Tax liability. <u>The bill limits the amount of credits that may be allowed each fiscal year to $5 M. The amount of credits that could potentially be claimed each year up to the limit, however, is indeterminable and depends on taxpayers qualifying for the federal NMTC and being certified for credits by the IEDC.</u> The credit applies only to qualified equity investment made after December 31, 2005, and can only be claimed beginning in tax year 2006. As a result of these circumstances, any fiscal impact from the credits likely would not arise before FY 2007.

Background: The nonrefundable tax credit is based on the equity investment held by a corporate or individual taxpayer, including a pass through entity, that is certified for the credit by the IEDC. (The credit calculation formula is described below.) The bill requires the IEDC to establish a program to certify qualified equity investment for the tax credit. The only equity investment that qualifies for the state credit is equity investment that qualifies for the federal NMTC. The formula for determining the credit amount is as follows:

Step (1): Determine the amount of the qualified equity investment that is:
(A) held by the taxpayer on the credit allowance date in the taxable year; and
(B) certified as a certified equity investment by the DTCD.
Step (2): Multiply the Step (1) amount by the applicable percentage for the credit allowance date.
Step (3): Multiply the Step (2) amount by:
(A) the tax credit adjustment factor approved by the DTCD; or
(B) 0.85, if clause (A) does not apply.

The applicable percentages, as defined in the bill, equal 1% for the first 3 credit allowance dates and 2% for the remainder of the credit allowance dates. The credit allowance date is the date on which the investment is initially made and the six annual anniversary dates immediately following the date of the initial investment. Therefore, this credit is allowed for 7 years, and the bill also allows the taxpayer to carry any excess credit forward for not more than 3 subsequent taxable years.

The tax credit is nonrefundable, and unused credit amounts may not be carried back. However, a taxpayer may carry forward any unused credit amount for up to three subsequent taxable years. For pass through entities, the credit may be claimed by shareholders, partners, or members in proportion to their distributive income from the pass through entity. The bill provides that in the event federal NMTCs are disallowed or recaptured by the IRS, the state credits for the same equity investment are terminated only to the extent the state credits are disallowed or recaptured by the IEDC.

Revenue from the AGI Tax on corporations, the Financial Institutions Tax, and the Insurance Premiums Tax is distributed to the state General Fund. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of the revenue is deposited in the Property Tax Replacement Fund. Since the tax credit is effective beginning in tax year 2006 for certified investment made beginning in 2006, and requires IEDC certification, the fiscal impact likely would not begin before FY 2007.

Information on the Federal New Markets Tax Credit: Section 45D of the Internal Revenue Code (IRC) allows the federal NMTC for a taxpayer who holds a qualified equity investment on the credit allowance date. The credit allowance date is the date on which the equity investment is initially made, and six anniversary dates each year thereafter. For each of those dates the entity receives a federal tax credit for the equity investment. A qualified equity investment means any equity investment in a qualified community development entity if: (1) the investment is a cash investment; (2) substantially used by the qualified community development entity to make qualified low-income community investments; and (3) such investment is designated for the purposes of this code section by the qualified community development entity.

A qualified community development entity is defined as any domestic corporation or partnership with the primary mission of serving, or providing investment capital for, low-income communities or persons. The entity must maintain accountability to residents of these low-income communities through representation on any governing board of the entity. These qualified community development entities are also required under the IRC to be certified by the Treasury Secretary.

Since 2002, allocations of creditable investment under the NMTC have been awarded by the U.S. Department of Treasury. These allocations represent the amount of investments that were designated as qualifying for the NMTC. Section 45D of the Internal Revenue Code limits the total amount of designated investments to $2 billion nationwide in 2005, and $3.5 billion nationwide in 2006 and 2007. In 2005, no entities located in Indiana received allocations. However, three entities from out of state received allocations and list Indiana as part of their service area. In 2003-2004, two Indiana entities received allocations totaling $75 M. In 2002, two Indiana entities received allocations totaling $6 M.

Explanation of Local Expenditures: *Local CDFI*s: The bill authorizes a county or municipality to apply to the IEDC for designation as a Local CDFI. (See *Explanation of State Expenditures* for information on CDFIs.) The bill authorizes Local CDFIs to do any of the following: (1) promote community development; (2) provide loans, investments, banking services, or development services in a targeted investment areas or to targeted populations (see *Explanation of State Expenditures* for definitions); (3) perform activities consistent with the goals of the federal CDFI Program; and (4) perform any other activity that Local CDFIs are allowed to carry out. A county or municipality also may establish a foundation for designation as a Local CDFI to perform these functions.

The bill authorizes a county or municipality to use any money or tax revenue it receives to carry out the purposes of a Local CDFI.

Explanation of Local Revenues:

State Agencies Affected: Indiana Economic Development Corporation; Department of State Revenue.

Local Agencies Affected: Counties and municipalities.

Information Sources: U.S. Department of the Treasury, http://www.cdfifund.gov/programs/programs.asp?programID=5#2

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