

# 2019 Income Tax Credit Review

## Joint Legislative Income Tax Credit Review Committee

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# 2019 Credit Reviews

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- ☐ Annually reviews credits as determined in statute
- ☐ This year's review includes:
  - 1) Healthy Forest Enterprise Employment Credit
  - 2) Agricultural Pollution Control Equipment Credit
  - 3) Agricultural Water Conservation System Credit
  - 4) Qualified Facility Credit
  - 5) Credit for Renewable Energy Investment and Production for Self-Consumption by International Operations Centers
  - 6) Credit for Corporate Contributions to School Tuition Organizations for Displaced or Disabled Students
- ☐ All but credits 4) and 5) have been previously reviewed by the committee

## Summary of Prior Credit Reviews

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- ☐ Between 2002 and 2015, Committee reviewed 33 credits
- ☐ Committee did not convene in 2016, 2017, and 2018
- ☐ Between 2002 and 2015, Committee recommended 16 credits to be repealed
- ☐ 1 of the 16 credits was repealed by Legislature

## Role of the Committee

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- ☐ Determine original purpose of credit
- ☐ Establish standards for evaluating and measuring success or failure of credit
- ☐ After review process, recommend whether credit should be amended, repealed or retained

# Standards for Evaluating Credit

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- ☐ History, rationale and revenue impact of credit
- ☐ Benefits of credit in terms of measurable economic development, investments and jobs
- ☐ Complexity of credit in terms of application, administration and approval process

## Confidential Taxpayer Information

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- ☐ Statute authorizes DOR to disclose confidential “statistical information” to the Committee, JLBC Staff and Legislative Staff
- ☐ DOR considers credit information confidential if:
  - credits were claimed by 3 or fewer taxpayers, or
  - a single taxpayer used more than 90% of total credits
- ☐ Agricultural water conservation system credit is the only credit on the 2019 review schedule that does not include confidential information

# Issues Affecting Evaluation

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- ☐ Lack of performance measures
- ☐ Certain costs and benefits can be difficult to quantify

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# **Healthy Forest Employment Tax Credit**



# Healthy Forest Employment Credit

## - Summary

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- ☐ Cost – \$0 for both the corporate and individual income tax credit in FY 2019.
  - The individual credit was most recently claimed in FY 2018, however, credit use that year cannot be publicly released due to confidentiality laws.
- ☐ Purpose – Provide incentive to help establish businesses that promote forest health.
- ☐ Complexity – Not difficult to use but requires significant paperwork for application and reporting purposes.
- ☐ Performance Measures – Exist in statute as a result of 2009 Committee review.

# Healthy Forest Employment Credit

## - Description

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- ☐ Employment credit is based on the net increase in the number of qualified employment positions created and filled.
- ☐ Amount of credit per employee depends on employee's wage and year of employment:
  - 1/4 of employee's wage in the 1st year of employment up to \$500
  - 1/3 of wage in the 2nd year of continuous employment up to \$1,000
  - 1/2 of wage in the 3rd year of continuous employment up to \$1,500
- ☐ Taxpayer cannot claim more than 200 qualified employment positions in any given tax year.
- ☐ Employee must be compensated at a wage at least equal to the county wage as computed by the Arizona Department of Economic Security.

# Healthy Forest Employment Credit

## - Description of Credit (Continued)

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- ☐ To qualify for the credit use, the employer must provide health insurance and pay for at least 25% of premium cost in the employee's 3rd year of employment, 40% in the 4th year, and 50% in the 5th year.
- ☐ Prior to using any tax incentive under the program, a business must first be approved ("certified") by ACA. (A total of 8 businesses certified in calendar year 2018.)
- ☐ Certified business must submit an annual report to ACA and reapply for certification every 5 years.
- ☐ Besides the tax credit, the program also offers other incentives related to use fuel, sales and property taxes.
- ☐ Credit is nonrefundable with a 5-year carry-forward.

# Healthy Forest Employment Credit

## - Amount of Credits Taken and Number of Claimants

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- ☐ No corporate tax credit has been claimed since 2009. The extent to which the credit was used during that year cannot be publicly released due to confidentiality laws
- ☐ The individual employee tax credit was most recently claimed in FY 2018, however, the extent to which the credit was used that year cannot be publicly released due to confidentiality laws.

# Healthy Forest Employment Credit

## - Benefits to the Arizona Economy

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- ☐ Impact on the state's economy is likely negligible due to the limited use of the credit.
- ☐ Certified businesses have indicated that the incentives program was an important factor in the decision to locate, expand, or remain in the state.
- ☐ Beginning in 2011, ACA has reported to JLBC on the total weight of harvested, processed and/or transported forest materials.
  - In 2018, 8 certified businesses harvested, processed and/or transported a combined 619,000 tons of forest materials.
  - None of the businesses reported net new employment positions for the income tax credit program.

# Healthy Forest Credits

## - Performance Measures

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- ☐ The following performance measures were adopted as a result of Committee review in 2009:
  - Requirement to report quantity of qualifying forest products harvested, processed, or transported for commercial use.
  - Total statewide number of new jobs created as a result of the program.
- ☐ The Committee last reviewed the credit in 2014 and recommended that the individual and corporate income tax credit for healthy forest employment be eliminated.

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# **Agricultural Pollution Control Tax Credit**

# Agriculture Pollution Control Credit

## - Summary

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- ❑ Cost – \$0 in FY 2019 for the corporate credit and \$16,225 in FY 2019 for the individual credit.
  - In FY 2019, 4 individuals claimed the individual credit.
  - The most recent corporate claim was made in 2006.
- ❑ Purpose – to mitigate costs incurred by farmers and ranchers to comply with environmental regulations.
- ❑ Complexity – simple to use and administer.
- ❑ Performance Measures – none in statute.



# Agriculture Pollution Control Credit

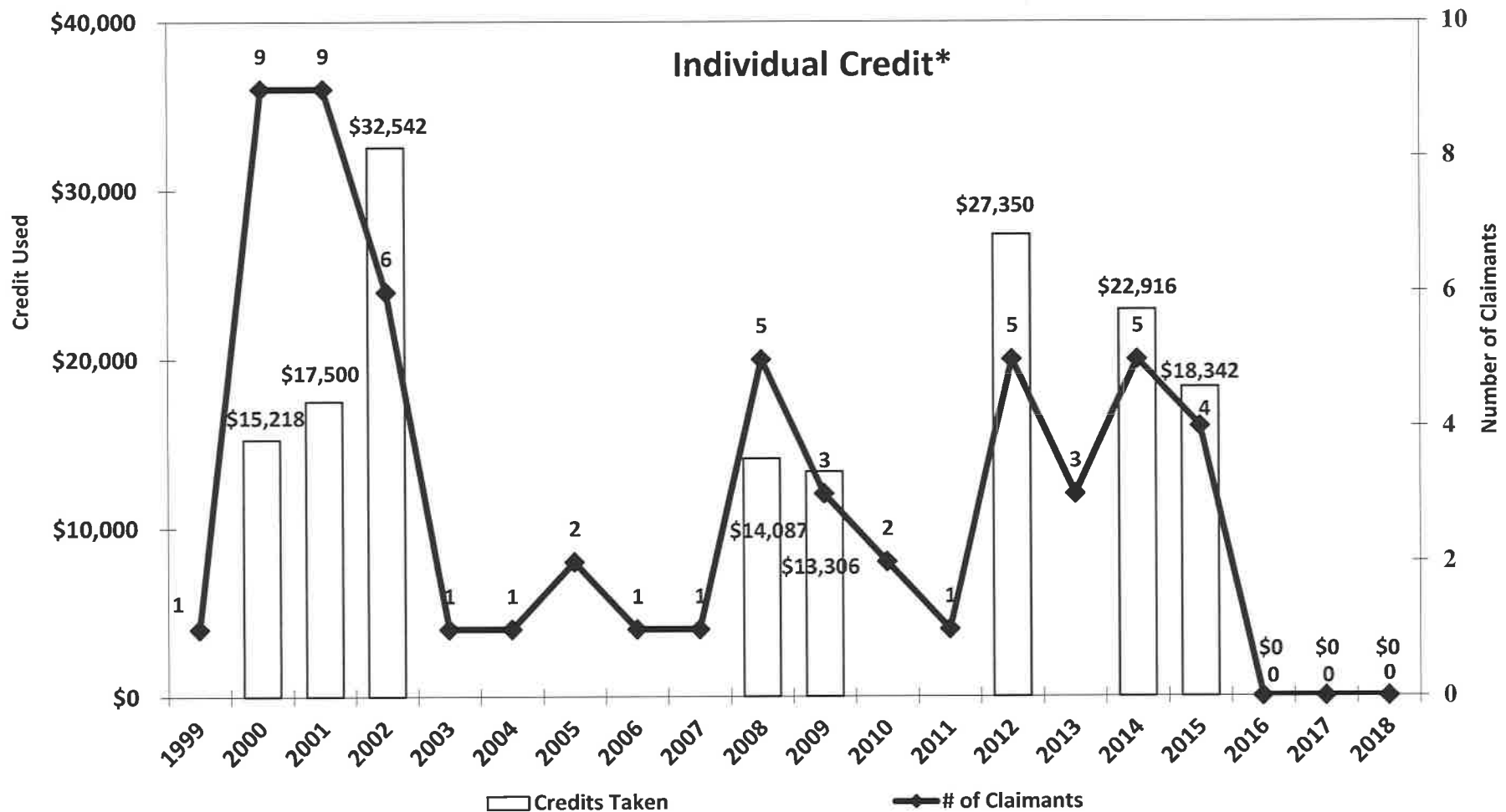
## - Description of Credit

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- ☐ The credit is for expenses incurred to acquire agricultural pollution control equipment.
- ☐ Example of equipment that may qualify for the credit is dust filters in cattle feed yards.
- ☐ The credit is equal to 25% of the cost of equipment up to a maximum of \$25,000.
- ☐ Credit is nonrefundable.
- ☐ Carry forward is 5 years.

# Agriculture Pollution Control Credit

## - Amount of Credits Taken and Number of Claimants



\* No data publicly released by DOR with respect to credit use for tax years 1999, 2003-2007, 2010-2011, and 2013.

# Agriculture Pollution Control Credit

## - Benefits to the Arizona Economy

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- ☐ Impact on the state's economy is likely negligible due to the limited use of the credit.
- ☐ Credit may have a small positive impact on the environment insofar as it induces taxpayers to reduce pollution that would not occur in the absence of the credit.

# Agriculture Pollution Control Credit

## - Potential Performance Measures

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- ☐ Type of equipment purchased and its related environmental impact.
- ☐ Number of other states where a taxpayer receives a comparable credit.
- ☐ Last reviewed in 2014.
- ☐ Committee recommended that the tax credits be eliminated.

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# **Agricultural Water Conservation Tax Credit**

# Agriculture Water Conservation Tax Credit

## - Summary

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- ☐ Cost – \$2.7 million in FY 2019.
  - 108 claims filed by individual taxpayers in FY 2019.
  - Corporate credit was repealed in 2000.
- ☐ Purpose – mitigate cost incurred by farmers and ranchers to comply with water conservation requirements under the 1980 Groundwater Management Code.
- ☐ Complexity – simple to use and administer.
- ☐ Performance Measures – none in statute.

# Agriculture Water Conservation Tax Credit

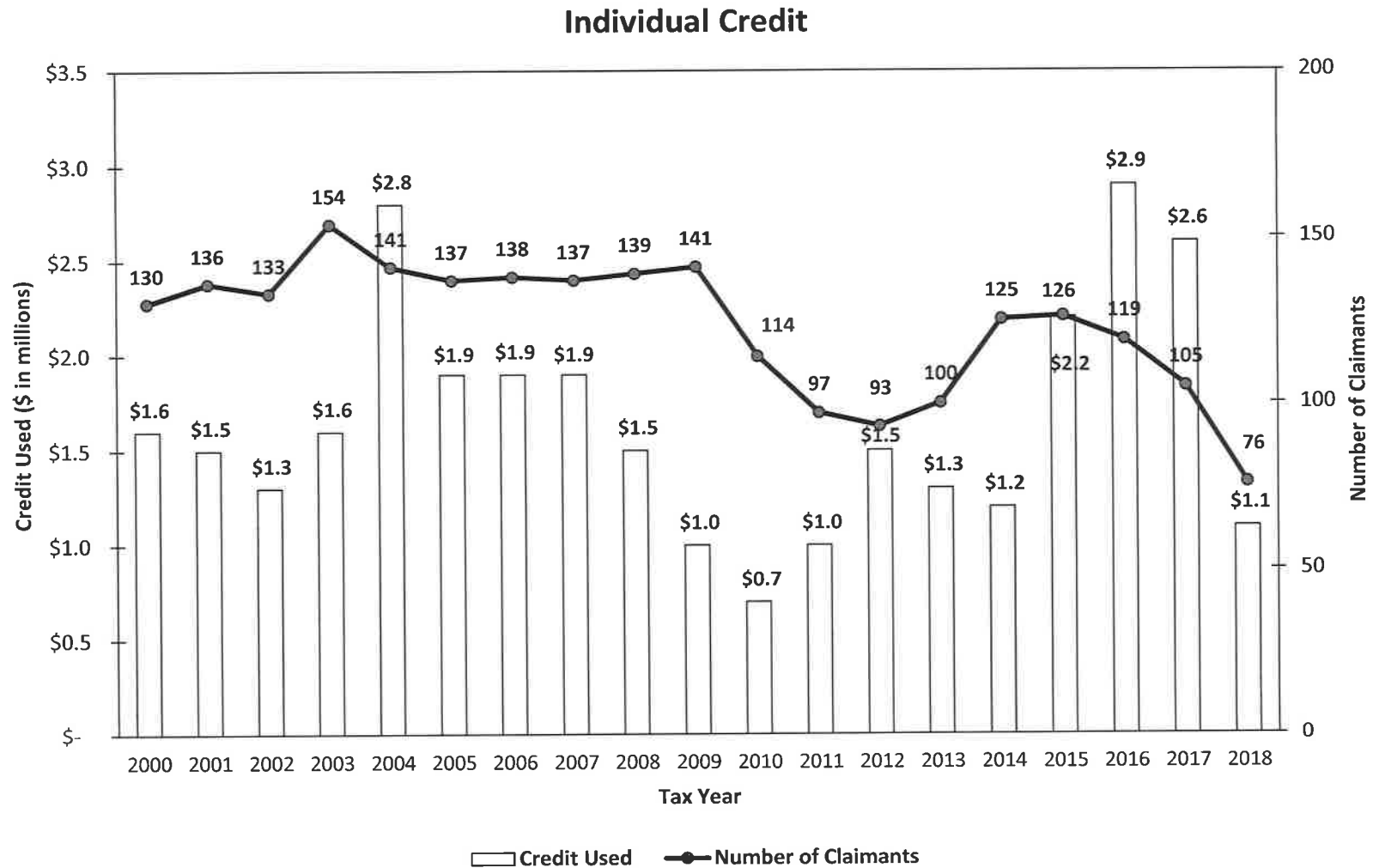
## - Description of the Credit

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- ☐ The credit is equal to 75% of expenses for the purchase and installation of an agricultural water conservation system.
  - Credit is not capped
- ☐ Examples of water conservation systems: sprinklers, pipes, water pumps, and computer aided irrigation and water management systems.
- ☐ Taxpayer must have a conservation plan on file with the USDA to qualify for credit.
- ☐ Credit is non-refundable; carry forward is 5 years.

# Agriculture Water Conservation Tax Credit

## - Amount of Credits Taken and Number of Claimants





# Agricultural Water Conservation Tax Credit

## – Benefits to the Arizona economy

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- ☐ Credit may have a positive impact on the environment with reduced water usage that would not occur absent of the credit.
- ☐ Credit may enhance Arizona's competitiveness relative to other states by reducing cost of production.
- ☐ No data is available to quantify potential impact on the state's economy.

# Agricultural Water Conservation Tax Credit

## – Potential Performance Measures

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- ☐ A requirement to report on the reduction in water usage as a result of the installation of a qualified water conservation system.
- ☐ Number of other states where a taxpayer receives a comparable credit.
- ☐ Last reviewed in 2014.
- ☐ Committee recommended that the credit be eliminated in 2014.

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# **Qualified Facility Tax Credit**

# Qualified Facility Credit

## - Summary

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- ☐ Cost – \$26,000 for the individual credit in FY 2019
  - The most recent individual claim was made in FY 2018; a total of 6 claims since the credit's inception have been made.
  - Corporate claims not released due to confidentiality rules.
- ☐ Purpose – expanding or locating a qualified facility in Arizona; create employment
- ☐ Complexity – moderate due to procedural requirements
- ☐ Performance Measures – none in statute

# Qualified Facility Credit

## - Description of the Credit

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- ❑ A “qualified facility” is a building that has 80% or more of its space for manufacturing, research and development, or headquarters
  - Minimum capital investment of \$250,000 to locate or expand a qualified facility in Arizona
  
- ❑ New “qualified job” requirements
  - At least 51% of workers must be paid at least 125% of state median wage (100% in rural locations)
  - Company must offer to pay at least 65% of health insurance premiums for full-time workers
  - New hire must not have worked for the company within the last 12 months

# Qualified Facility Credit

## - Calculation of the Credit

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- ☐ The credit is the lesser of:
  - 10% of the qualified facility capital investment
  - \$20,000 per qualified job created at the facility
  - \$30 million per taxpayer
- ☐ The credit is refundable
  - Can exceed taxpayer's liability
- ☐ The credit must be taken over 5 equal installments
- ☐ The credit is capped at \$70 million per calendar year

# Qualified Facility Credit

## - Legislative Changes Since Inception

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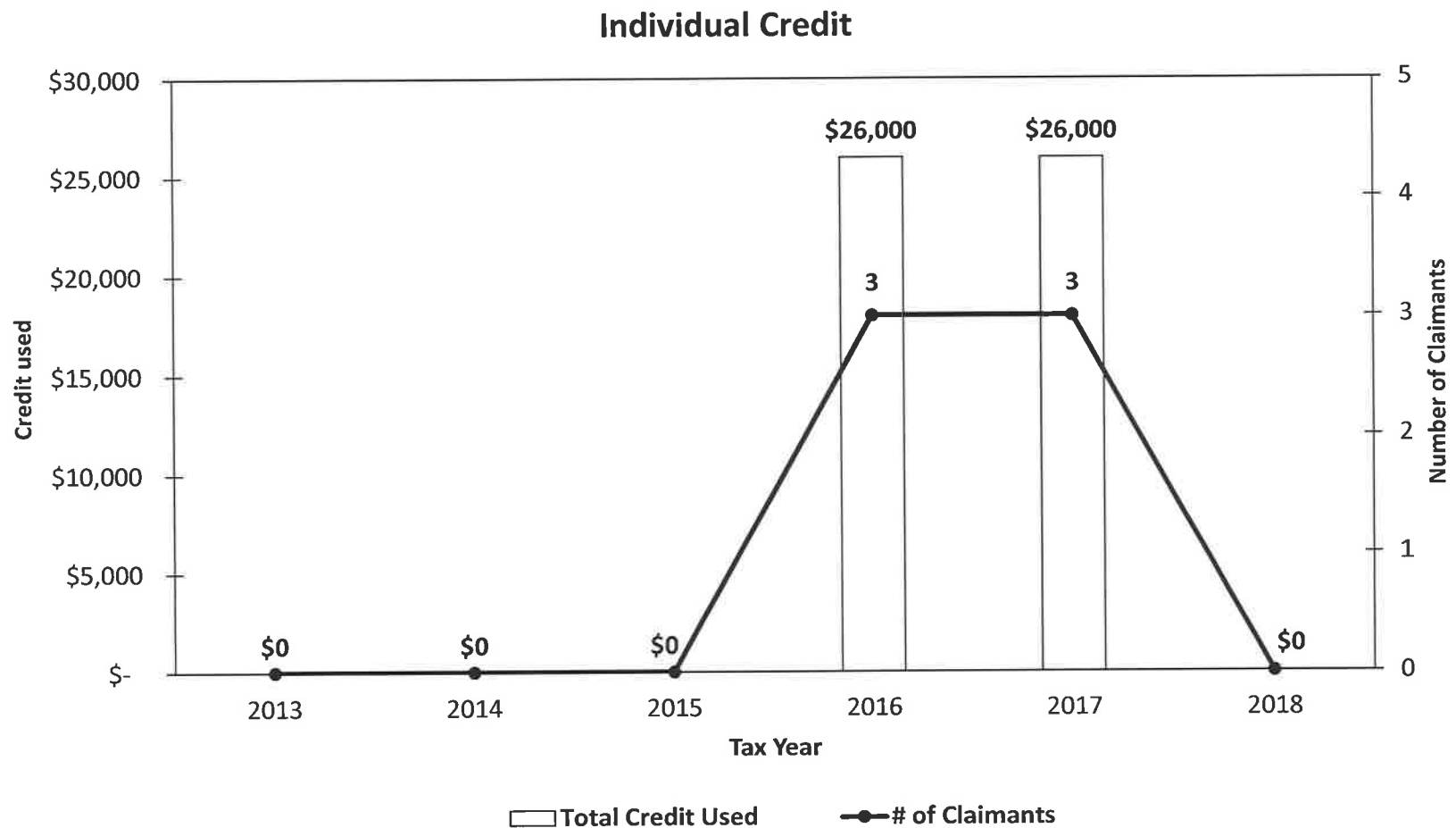
### ☐ Laws 2016, Chapter 372

- Reduced employer's required health insurance premium contribution from 80% to 65%
- Lowered rural wage requirement from 125% to 100% of the state median wage

☐ FY 2020: \$42,600/year to \$34,100/year

# Qualified Facility Credit

## - Amount of Credits Taken and Number of Claimants





# Qualified Facility Credit

## - Amount of Credits Taken and Number of Claimants

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Corporate Credit		
<u>Tax Year</u>	<u># of Claimants</u>	<u>Credit Used</u>
2013	0	0
2014	0	0
2015	NR	NR
2016	NR	NR
2017	5*	\$ 2,744,000*

\* indicates data is preliminary

NR indicates data is confidential and not released

# Qualified Facility Credit

## - Benefits to the Arizona Economy

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- ☐ Total of 13 projects by 11 companies post-approved for the credit
- ☐ Actual level of investments and job creation by these companies not reported
- ☐ Since minimum investment requirement per facility is \$250,000, at least \$3.25 million has been invested
- ☐ It is not known how many of the 13 projects would have been undertaken absent the credit

# Qualified Facility Credit

## - Potential Performance Measures

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- ☐ Number of new employees hired
- ☐ Total capital expenditures invested
- ☐ Committee has not previously reviewed this credit

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# **Credit for Renewable Energy Investment and Production for Self-Consumption by International Operations Centers (IOC)**

# Renewable Energy for Self-Consumption Credit

## – Summary

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- ☐ Cost – \$0 for the individual credit in FY 2015 – FY 2019. \$0 for the corporate credit in FY 2015 – FY 2018 (FY 2019 not reported due to confidentiality).
- ☐ Purpose – to reduce the carbon footprint by investing in and producing renewable energy for self-consumption.
- ☐ Complexity – application, administration and approval process of credit appears relatively simple.
- ☐ Performance Measures – none in statute.

# Renewable Energy for Self-Consumption Credit

## – Description of the Credit

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- ☐ The credit is for investment in new renewable energy facilities that produce energy for self-consumption by an International Operations Center (IOC).
- ☐ To qualify as an IOC, the taxpayer must meet the following 3 requirements:
  - Invest  $\geq$  \$100 million in renewable energy facilities by December 31, 2018.
  - Invest  $\geq$  \$1.25 billion in new capital assets within 10 years of IOC certification (minimum annual capital investment is \$100 million).
  - Use  $\geq$  51% of the energy produced for self-consumption by the 5<sup>th</sup> year the IOC is in operation.

# Renewable Energy for Self-Consumption Credit

## – Description of the Credit (cont.)

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- ☐ Credit amount is \$5 million per year for 5 years for each renewable energy facility, for a total of \$25 million.
- ☐ However, regardless of the number of renewable energy facilities, no single taxpayer can receive more than \$5 million per year, and \$25 million in total over 5 years.
- ☐ The maximum amount of credit approved for all taxpayers is \$10 million per year.
- ☐ Only 1 company qualified as an IOC before the statutory deadline of December 31, 2018.

# Renewable Energy for Self-Consumption Credit

## – Amount of Credits Taken and Number of Claimants

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- ☐ Individual income tax credit: No claims since the credit program's inception in 2014.
- ☐ Individual credit repealed in 2019.
- ☐ Corporate income tax credit: 1 claimant, beginning in TY 2016. Amount of credits taken not reported due to confidentiality.
- ☐ Credit amount is expected to be \$5 million per year for 5 years, for a total of \$25 million.



# Renewable Energy for Self-Consumption Credit

## – Benefits to the Arizona Economy

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- ❑ According to ACA's Annual Report, 1 company (Apple, Inc.) has been approved under the IOC program.
- ❑ According to a 2015 news release, Apple promised to invest \$2 billion over 10 years in a “command center,” which would result in 150 full-time jobs.
- ❑ Investment would also generate 500 construction jobs.
- ❑ JLBC Staff doesn't have the required data to determine to what extent these objectives have been met.

# Renewable Energy for Self-Consumption Credit

## – Potential Performance Measures

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- ☐ A requirement to report on:
  - Number of net new jobs created by the IOC
  - Percentage of electricity generated that is used for self-consumption by the IOC
  
- ☐ Committee has not reviewed this credit before

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# **Private School Tuition Organization (STO) Displaced/Disabled Pupil Scholarship Credit**

# Private STO Displaced/Disabled Credit

## - Summary

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- ☐ Cost – \$5.0 M in donations in FY 2017
  - actual credit usage may vary
- ☐ Purpose – assist parents with the cost of private school tuition for displaced or disabled pupils
- ☐ Complexity – simple to use for donors.  
Administration, reporting and oversight are time-consuming for STOs and DOR because of the number of students and STOs and data quality issues
- ☐ Performance Measures – none in statute

# Private STO Displaced/Disabled Credit

## - Description of Credit

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- ☐ Corporate and insurance premium income tax credit for contributions to a school tuition organization (STO):
  - charitable organization exempt from federal taxes
  - awards 90% of tax credit revenue for scholarships & grants
- ☐ Maximum credit allowed is \$5 million statewide:
  - no separate maximum for individual corporations, individuals (S-corporations), or insurers
  - DOR must preapprove credits, which provides “real time” data
  - cap reached for 1st time in FY 2015 and annually thereafter
- ☐ 18 STOs received contributions in FY 2017

# Private STO Displaced/Disabled Credit

## - Related STO Credits

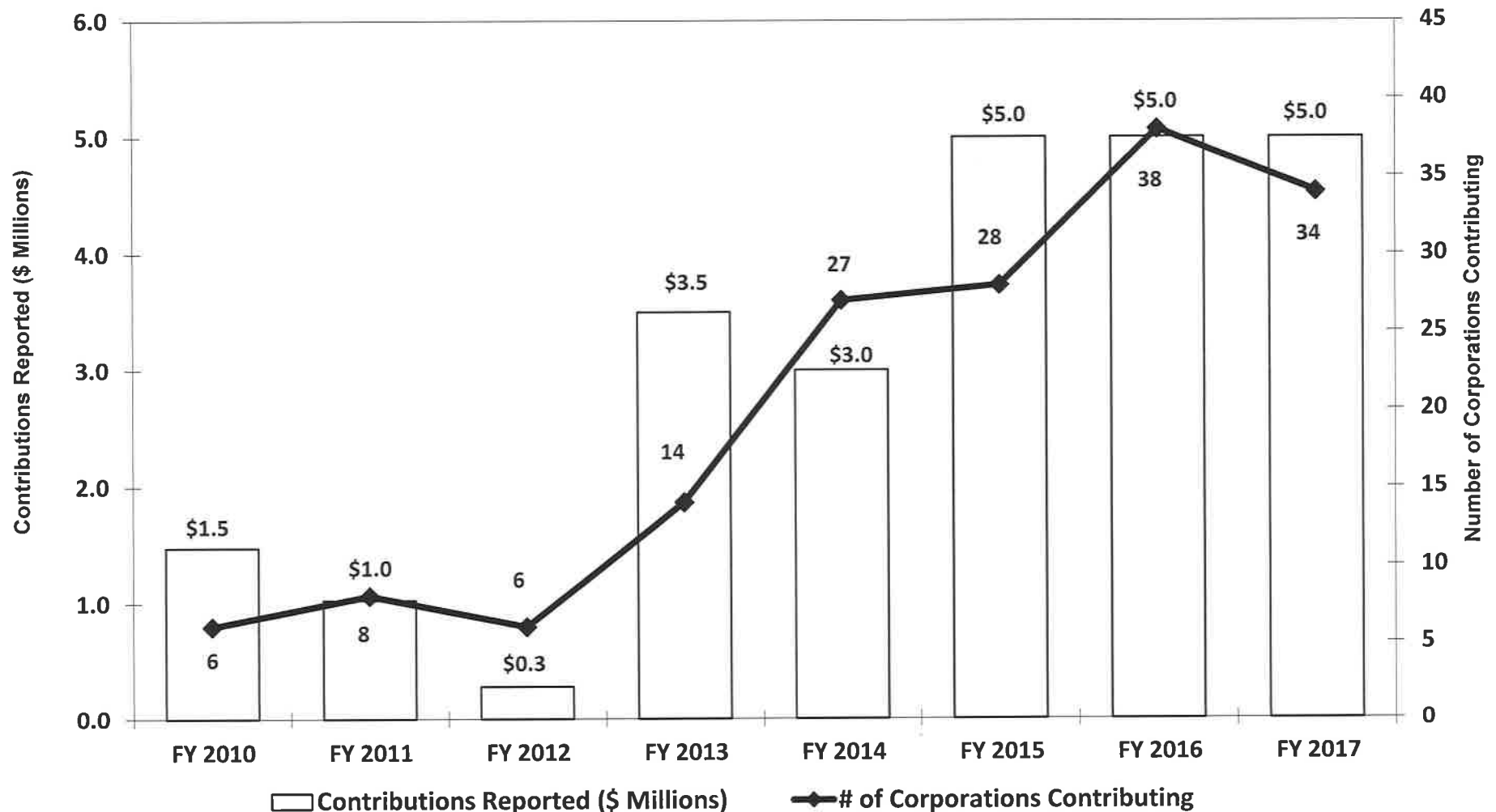
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Three other STO tax credits exist (none under review this year):

- ☐ Corporate & insurer “low income pupil scholarship” credit
  - scholarships for “low income” pupils
- ☐ Individual “original” STO credit
  - scholarships for private school students (not restricted to low income or displaced/disabled)
- ☐ Individual “switcher” STO credit
  - scholarships mainly for pupils who switch to private schools
  - donor must first take maximum “original” STO credit

# Private STO Displaced/Disabled Credit

- In FY 2017, Average Contribution was \$147,100



# Private STO Displaced/Disabled Credit

## - Impact on State Revenues

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- ☐ \$5.0 M in donations would result in \$(5.0) M state revenue loss if all donations resulted in credits
- ☐ Amount and timing of credits is uncertain because one tax year can cover 4 fiscal years
- ☐ Plus credits may be carried forward 5 years
- ☐ Credits claimed during FY 2019 = \$6,007,300
  - \$2,295,100 for corporations
  - \$3,448,100 for insurers
  - \$264,100 for individuals (S-corporations)



# Private STO Displaced/Disabled Credit

## - Impact on State K-12 Costs

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- ☐ Revenue loss is offset to the extent that credit allows students to attend private school who otherwise would have attended public school
  
- ☐ State K-12 Costs:
  - Operating – \$21,800 per ADM (estimated blended average for disabled & displaced pupils)
  - Capital – New construction and building renewal savings

# Private STO Displaced/Disabled Credit

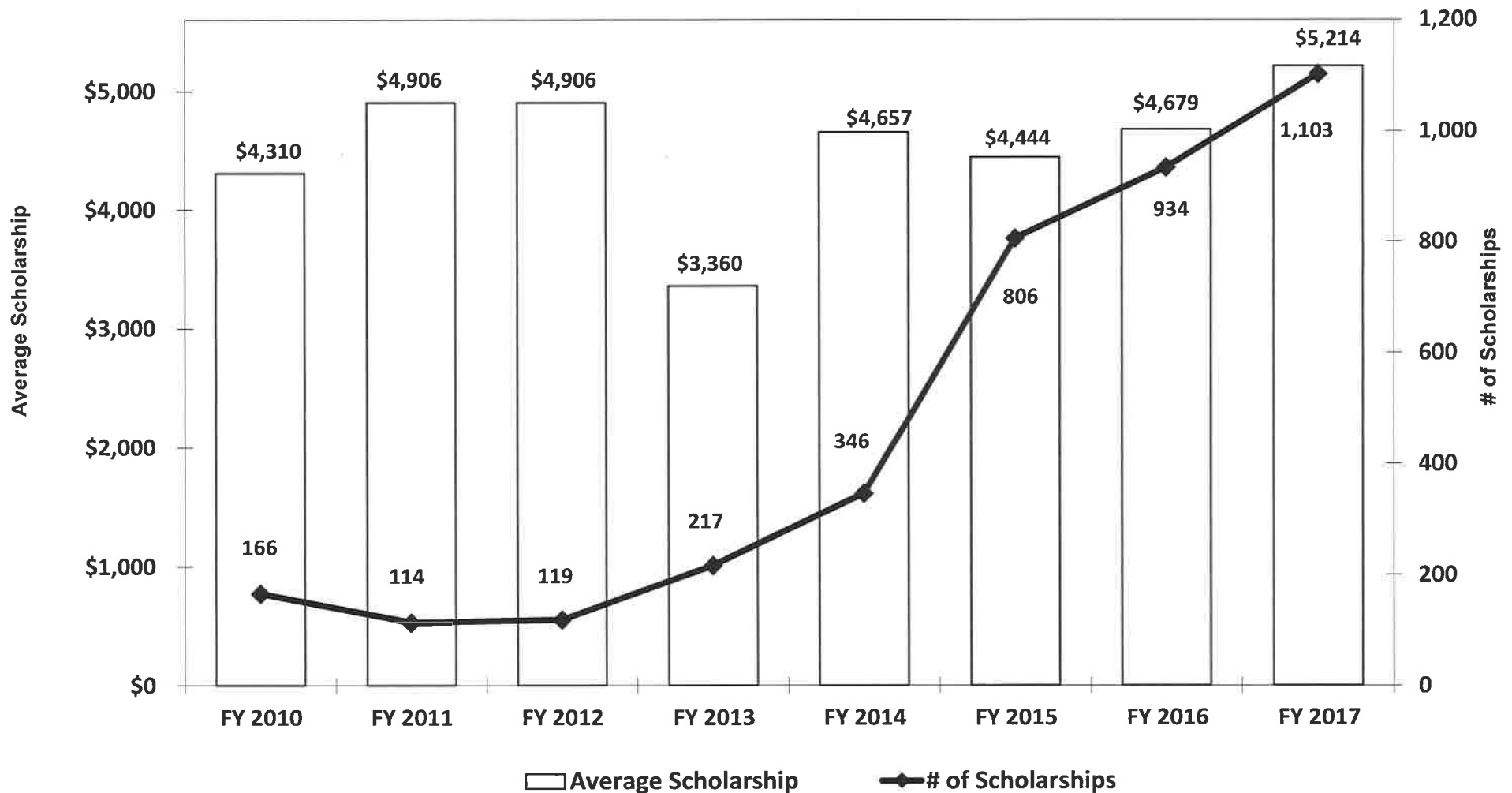
## - Impact on State K-12 Costs

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- ☐ No net long-term GF cost if tax credits of \$5.0 M per year (for example) reduced public school attendance by at least 230 pupils ( $\$5.0 \text{ M} \div \$21,800$  estimated average savings per pupil = 230 pupils)
- ☐ STOs awarded 1,103 displaced or disabled pupil scholarships in FY 2017 (duplicated count)
- ☐ No data on the proportion of scholarship recipients who otherwise would attend public schools

# Private STO Displaced/Disabled Credit

- In FY 2017, 1,103 Scholarships Awarded (Average = \$5,214)



# Private STO Displaced/Disabled Credit

## - Average Scholarship Funding and Tuition

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- ❑ 1,103 scholarships in FY 2017 versus 130,000+ displaced or disabled pupils in Arizona
- ❑ Each scholarships probably covers only about 25% of private school tuition costs for disabled pupils (\$5,214 average scholarship for FY 2017 versus \$21,800 estimated tuition cost based on estimated average state formula savings per participating student)

# Private STO Displaced/Disabled Credit

## - Potential Performance Measures

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- ☐ Percent of STO revenues retained for administrative costs
- ☐ Percent of private school tuition paid for with award funding