DEPARTMENT OF AUDITS AND ACCOUNTS

270 Washington St., S.W., Suite 1-156
Atlanta, Georgia 30334-8400

Greg S. Griffin
STATE AUDITOR
(404) 656-2174

December 20, 2016

Honorable Dar'shun Kendrick
State Representative
404-E Coverdell Legislative Office Building
Atlanta, Georgia 30334

SUBJECT: Fiscal Note
House Bill (LC 39 1437ER)

Dear Representative Kendrick:

The bill would amend the existing qualified investment tax credit under O.C.G.A. §48-7-40.30 in two material respects. The definition of "qualified investment" would be expanded to include brokered investments where a fee or commission is paid and "sophisticated" investors would be eligible to take the credit.

According to Georgia State University's Fiscal Research Center (FRC), both changes would "tend to increase the cost of the credit above current law trends, but there is no clear basis for making a precise estimate as to the magnitude of these effects." Instead, FRC created a baseline projection for the existing credit and compared that amount to the current law's $5 million annual cap. The difference is the maximum amount of the credits available for investments allowed by this bill.

As shown in Table 1, maximum revenue loss is estimated at $2.76 million in fiscal year 2020. The amounts are based on investments made on or after July 1, 2017 and recognize that the credit is available only for investments made through calendar year 2018.

Table 1. State Revenue Effects of LC 39 1437ER

($ *millions*)	**FY 2018**	**FY 2019**	**FY 2020**	**FY 2021**	**FY 2022**
Upper Bound	$0	$0	$2.76	$3.15	$0.47

Research did not indicate that the bill would have an impact on state agency expenditures.

Sincerely,

Greg S. Griffin
State Auditor

Teresa A. MacCartney, Director
Office of Planning and Budget

GSG/TAM/mt

Analysis by the Fiscal Research Center

Under current law, investments on which a commission or fee is paid to a broker or other intermediary for solicitation or offering of the investment are not eligible for the credit. Under the proposed amendment, such investments would be eligible for the credit, but only to the extent of funds invested in the qualified business, net of any fees or commissions. This change would likely serve to increase the amounts of qualified investments made, compared to trends under current law, as brokers would be motivated to educate potential investors about the availability of the credit and to raise larger sums for qualified businesses.

Current law also limits the credit to investors who meet Securities and Exchange Commission requirements as a qualified investor, among which are certain net worth and income thresholds the investor must meet. Qualified investors must also be natural persons or pass-through investment entities with no more than $5 million of capital and no institutional investors. Venture capital and hedge funds, or similar funds, with institutional investors are not eligible. By adding sophisticated investors to those eligible, such funds, institutional investors, and operating business entities would become eligible, provided only that they possess "sufficient knowledge and experience in financial and business matters which make him or her capable of evaluating the merits and risk of the prospective investment." This change would serve to open the credit to larger and more sophisticated investors who might be expected to qualify for additional, larger credits above the current law baseline.

The Department of Revenue (DOR) reports the following with regard to the credit:

Table 2. Business Registrations and Investments by Calendar Year Made

Calendar Year	2011	2012	2013	2014	2015
Businesses Registered	55	66	49	55	70
Investors Approved*	12	24	42		
35% of Amount Invested	$261,105	$694,517	$941,437		

* Approval of investors and investments for the credit occurs in the year the credit is first claimed, two years after the investment.

Based on trends in the reported data for business registrations, amounts invested, and credits utilized, baseline projections of credits expected to be earned and the balance available to be claimed for newly-eligible investments are as shown in Table 3. Further assumptions made for these projections include that:

- the number of businesses registering grows at 5 percent per year;
- the number of investors grows with businesses registered based on the ratio of 42 investors to 49 businesses in calendar 2013;
- the average credit earned (35 percent of eligible investment) is assumed to be $25,000 in 2014 (average of prior three years was $24,400), growing at 2 percent annually thereafter;
- credits available for investments made eligible by the proposed amendments are the difference between baseline credits earned and the $5 million per year cap;

- utilization of these newly eligible credits against tax liability the year claimed is projected at 85 percent of the earned credit with the balance carried forward and utilized the following year; and
- credits utilized in a given tax year are assumed to impact tax collections in the fiscal year ending June 30 of the following calendar year.

Table 3. Baseline Projections
(*$ thousands*)

Investment Year	2016	2017	2018	NA
Tax Year	2018	2019	2020	2021
35% of Amount Invested	$1,638.6	$1,751.0	$1,867.2	NA
Balance Under Cap		$3,249.0	$3,132.8	NA
Balance Utilized		$2,761.7	$2,662.9	NA
Carryforward Utilized			$487.4	$469.9

NA = Not applicable.