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January 13, 2021

Honorable Sandra Scott
State Representative
611-D Coverdell Legislative Office Building
Atlanta, Georgia 30334

SUBJECT: Fiscal Note
House Bill (LC 44 1545)

Dear Representative Scott:

The bill would create an income tax credit for qualified investors who invest in the equity or subordinated debt of qualified women-owned businesses located in Georgia. It provides an individual income tax credit of 50 percent of the qualified investment, with investors receiving a credit equal to 25 percent of the qualified investment in the second tax year following the year in which the investments are made, 15 percent in the third tax year, and 10 percent in the fourth tax year. The credit is nonrefundable, but unused credits may be carried forward for up to 5 years. The credit limit for an individual is $100,000 per tax year, and the total aggregate limit of tax credits allowed by all taxpayers is $5 million per year. The bill does not include an effective date but is assumed to be effective beginning for tax year (TY) 2021.

This legislation is similar to the qualified investor tax credit provided by O.C.G.A. §48-7-40.30, but in addition to applying only to investments in women-owned businesses, this bill provides a larger tax credit (50 percent compared to 35 percent) and a higher tax credit maximum ($100,000 compared to $50,000) than the previous credit, which expired for new investment at the end of 2018.

Impact on State Revenue

Georgia State University's Fiscal Research Center (FRC) estimated that the bill would cost between $200,000 and $5 million in fiscal year 2024, the first year of any impact due to the delay in the ability of investors to claim the credit (see Table 1). Details of the analysis are provided in the attached appendix.

Table 1. Estimated State Revenue Effects of LC 44 1545

($ *millions*)	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
Upper-Bound Estimate	-	-	($5.0)	($5.0)	($5.0)
Low Estimate	-	-	($0.2)	($0.4)	($0.5)

Impact on State Expenditures

The Department of Revenue (DOR) would need additional funding of approximately $300,000 for four additional employees. These employees would conduct the certification and verification of investors and businesses, as well as the processing of the credit when claimed. One-time costs of $5,475 would be incurred for the computers and supplies for the employees.

Sincerely,

Greg S. Griffin
State Auditor

Kelly Farr

Kelly Farr, Director
Office of Planning and Budget

GSG/KF/mt

Analysis by the Fiscal Research Center

Key Provisions of the Tax Credit
The income tax credit created by LC 44 1545 would apply to qualified investors who invested in qualified women-owned businesses. The key terms and qualifications of the credit include:

- Qualified investors include 1) individual persons who are residents or non-resident taxpayers of Georgia, or 2) a pass-through entity "which is formed for investment purposes, has no business operations, has committed capital under management [no greater] than $5 million, and is not capitalized with funds raised …" from institutional investors. Hedge funds, or venture capital or commodity funds with institutional investors do not qualify.
- Qualified investments are cash investments in the common or preferred equity, or subordinated debt of a qualified business.
- Qualified businesses are businesses 1) organized less than five years before a qualifying investment is made, 2) having no more than 20 employees, 3) having had no more than$500,000 of revenue in any year, 4) having raised no more than $1 million to date in equity or debt, excluding bank loans, 5) that have not utilized the film tax credit described in O.C.G.A. §48-7-40.26, and 6) are not primarily engaged in:
    - real estate;
    - gambling;
    - natural resource extraction;
    - financial, brokerage, or investment activities or insurance; or
    - amusement, recreation, athletic or fitness activities for which an admission or membership is charged.

  Qualified businesses must register and be certified by the revenue commissioner as a qualified business prior to accepting a qualified investment and must renew their registration annually to remain a qualified business.
- Credits are allowed beginning in the second tax year following the tax year of the investment at a rate of 25 percent of the qualifying investment. In the third and fourth years following the investment, credits in the amount of 15 percent and 10 percent of the investment, respectively, may be taken. Credits are subject to a maximum amount of $100,000 per qualified investor per year for all such qualified investments, whether made directly or through a pass-through entity.
- The aggregate credits available in any year is capped at $5 million. Investors are required to apply for the credit between September 1 and October 31 in the year in which they are first eligible to claim the credit. If eligible applications exceed the annual cap, amounts of credits approved are to be prorated among eligible applicants for that year.
- The credit is not refundable, but unutilized credits may be carried forward for up to three years after the year the credit is first claimed (five years from the end of the taxable year in which the qualified investment is made).
- Credits are subject to recapture if 1) the investor or an immediate relative becomes an active participant in the operation of the business, whether as an employee, contractor, or otherwise, providing services for compensation (not including stock, stock options or equivalent) within two years of the qualifying investment; or 2) the business redeems or repays any principal of qualifying equity or debt investments within five years.

Comparisons to the Qualified Investor Tax Credit
This bill is similar to the qualified investor tax credit provided by O.C.G.A. §48-7-40.30, also called the "angel investor credit", with the key difference being that this bill applies only to women-owned businesses. This bill is also more generous on four dimensions:

- This bill allows qualified businesses to be organized up to five years before a qualified investment is made, compared to three years under O.C.G.A. §48-7-40.30.
- This bill provides a higher total tax credit: a total of 50 percent of the qualified investment, spread over three years, compared to 35 percent.
- This bill allows a higher maximum individual credit: $100,000 per year compared to$50,000.
- The angel investor credit also had stricter limitations on the business activities allowed by qualified businesses. Specifically, the activities allowed by this bill that were not eligible under O.C.G.A. §48-7-40.30 include:
  - Construction
  - Retail sales
  - Professional services

The last year in which qualified investments could be made under the angel investor credit was 2018, but the state's experience with that credit, together with any material differences in terms with the proposed credit, guides the analysis herein.

Estimation Methodology and Assumptions
Data on angel investment activity are limited and no data specific to Georgia are available. Thus, national data on angel investment activity, including angel investment in women-owned businesses, from the Center for Venture Research at the University of New Hampshire (CVR), Crunchbase, and others, were used to generate national estimates. These estimates were shared down to Georgia based on the share of venture capital investment captured by Georgia businesses, according to PricewaterhouseCoopers' MoneyTree report. In total, three different methods were used.

Method 1: data from CVR on the proportion of women-owned companies seeking angel investment, the "yield rate" or share of those ventures receiving funds, and the average investment size were used to estimate the amount of angel investment dollars received by women-owned businesses.

Method 2: a Forbes magazine estimate of the proportion of angel-backed companies owned by women in 2017 and the CVR estimate of total amount of angel investment in the United States were used to estimate the amount received by women-owned businesses in total.

Method 3: data from Crunchbase, a venture capital database and news website, on the proportion of venture capital investment captured by women-owned businesses was applied to total angel investment amounts to estimate the amount of angel investment in women-owned businesses.

Estimates for 2019 under these three estimation methods, shared down to Georgia, ranged from about $30 million to more than $77 million, averaging $52 million. Investment of only $30 million per year, if the businesses and investors meet the qualifying requirements, would generate $7.5 million per year of credits two years after the investment, $4.5 million the following year, and $3.0 million in the fourth year. Thus, it is concluded for purposes of the upper-bound estimates that the $5 million annual cap on total credits would be reached each year, beginning CY 2023, and reducing state revenues by the same amount annually, beginning FY 2024.

Data on lost revenue from the existing angel investment credit, however, suggest that participation has been far lower than estimates based on the number of angel-backed businesses in Georgia would suggest. Because of this, a different methodology was applied for the low-case estimate.

Department of Revenue (DOR) data on the amounts of credits preapproved and the implied amounts of qualifying investment made under the existing angel investor credit for the last five investment years under O.C.G.A. §48-7-40.30 are provided in Table 2 below, along with DOR-reported utilization of the credit by tax year.

Table 2. Credits Preapproved and Utilized, and Implied Qualifying Angel Investments

TY of Investment	**2014**	**2015**	**2016**	**2017**	**2018**
TY of Credit Approval	**2016**	**2017**	**2018**	**2019**	**2020**
Businesses Registered	55	70	27	39	39
Investors Approved	81	31	30	36	
Credits Preapproved	$889,686	$553,742	$557,741	$528,253	$1,005,253
Credits Utilized	$586,784	$549,466	$425,280	NA	NA
% of Preapproved	66%	99%	76%		

Sources: DOR and FRC calculations

Estimated qualifying angel investment for TY 2018 is then adjusted based on the national proportion of angel-backed companies owned by women (24 percent according to Forbes) to estimate amounts of investment made in women-owned businesses under the terms of the angel investment credit.

This estimate of qualifying investment was then increased to account for increased participation resulting from the more generous terms of this bill: specifically, the larger credit amounts and the fewer restrictions on eligible businesses. Data from the Center for Venture Research indicates that the retail sector accounted for 6 percent of angel investment in 2019, so the amounts of qualifying investment were adjusted upwards to account for this addition. Then the amounts were increased by an additional 25 percent to account for the other eligible sectors (construction and professional services), as well as the increased participation expected due to the larger credit size, compared to the existing tax credit. Finally, actual utilization of credits each tax year are estimated based on the relative amounts of utilized and preapproved credits in recent years under the angel investor credit, about 88 percent in TY 2017-18 (the latest two years available).

This base year estimate of investment that would qualify for and utilize the proposed credit is projected forward from 2018 based on an estimate of linear trend growth in angel investment in women-owned businesses made using CVR data for 2010-2019, about 3.8 percent annually. Resulting projections of qualifying investment, and credits generated and utilized, are shown in

Table 3. Credits utilized are assumed to impact state revenues in the fiscal year beginning in the given tax year.

Table 3. Projected Low-Case Qualifying Investment and Tax Credits under LC 44 1545
($ *thousands*)

TY of Investment	**2021**	**2022**	**2023**	**2024**	**2025**
TY of Credit Approval	**2023**	**2024**	**2025**	**2026**	**2027**
Qualifying Investment	$1,020	$1,059	$1,098	$1,140	$1,183
Credits Earned	$255	$418	$536	$556	$577
Credits Utilized	$224	$367	$470	$488	$506