

**1999 HOUSE FINANCE AND TAXATION**

**HB 1413**

1999 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1413

House Finance and Taxation Committee

Conference Committee

Hearing Date January 27, 1999

Tape Number	Side A	Side B	Meter #
1	x		0.5
Committee Clerk Signature <i>Jamie Stein</i>			

Minutes:

REP. BELTER Opened the hearing.

REP. JIM POOLMAN, DIST. 42, Introduced the bill. We are always looking for ways to bring business to North Dakota and create new businesses in North Dakota and create opportunities for the people in our state. A few sessions ago, the legislature created a seed tax credit program. It encourages private investment in businesses in North Dakota. Presented an E-mail from Randy Brown of Grand Forks, also an editorial from the Grand Forks Herald, plus an overview of the seed capital investment income tax credit.

RICK CLAYBURGH, STATE TAX COMMISSIONER, Testified in support of the bill.

In support of the bill for many reasons. This is another opportunity to give private investor in North Dakota the incentive to invest in business in North Dakota. The fiscal note is limited.

We are looking for technology based companies to house themselves in North Dakota, and this is the opportunity. We can administratively handle any issue that you give us on the short form.

We have lost control of the short form, we are trying to keep it to a single page. With technology and some of the changes that are occurring, we will have to make some changes on the short form, but we will still try to maintain a single page.

JIM MELLAND, CENTER FOR INNOVATION, Testified in support of the bill. This bill was originally passed in 1993, and it was made available on the long form. Since that time, no one has taken advantage of it. From our perspective, working with small companies and start up companies, raising capital is the primary problem they face. Talked about a federal program sponsored by the Small Business Administration, which is called the Access to Capital Electronic Network. Thirty eight states are currently using this FBA sponsored program. North Dakota has just joined. In trying to determine our market for this program, we have found there are approximately 12,000 qualified investors in North Dakota. A qualified investor is someone who has an income of one hundred thousand dollars per year and a net worth in excess of one million dollars. The passage of putting the seed capital tax credit on the short form, we believe, will be an added incentive for these investors to concentrate on investments in North Dakota.

VIVIAN GWIN, DAKOTA AERO MANUFACTURERS, Testified in support of the bill. See written testimony.

BRUCE GJOVIG, CENTER FOR INNOVATION, Submitted written testimony. See attached copy.

With no further testimony, the hearing was closed.

COMMITTEE ACTION 1-27-99, Tape #2, Side A, Meter #1.6

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House Finance and Taxation Committee

Bill/Resolution Number Hb 1413

Hearing Date January 27, 1999

REP. BELTER Asked for discussion regarding the bill because of the large fiscal note.

REP. WARNER Questioned whether the short-form can work, if the long-form does not.

REP. BELTER Stated the bill would be held to act on at a later date, he asked committee members to have amendments drafted to the bill if they wanted to.

COMMITTEE ACTION 2-8-99, Tape #2, Side A, Meter #14.0

REP. GROSZ Made a motion for a DO NOT PASS.

REP. RENNERFELDT Second the motion. MOTION CARRIED.

10 Yes 4 No 1 Absent

REP. RENNERFELDT Was given the floor assignment.

## FISCAL NOTE

(Return original and 14 copies)

Bill/Resolution No.: HB 1413

Amendment to: \_\_\_\_\_

Requested by Legislative Council

Date of Request: 1/20/99

1. Please estimate the fiscal impact (in dollar amounts) of the above measure for state general or special funds, counties, cities, and school districts. Please provide breakdowns, if appropriate, showing salaries and wages, operating expenses, equipment, or other details to assist in the budget process. In a word processing format, add lines or space as needed or attach a supplemental sheet to adequately address the fiscal impact of the measure.

**Narrative:** If enacted, HB 1413 is expected to reduce state general fund revenues by \$500,000 in the 1999-2001 biennium.

2. **State fiscal effect in dollar amounts:**

	1997-99 Biennium		1999-2001 Biennium		2001-03 Biennium	
	General Fund	Other Funds	General Fund	Other Funds	General Fund	Other Funds
<b>Revenues</b>			-\$500,000			
<b>Expenditures</b>						

3. What, if any, is the effect of this measure on the budget for your agency or department:

- a. For rest of 1997-99 biennium: \_\_\_\_\_  
**(Indicate the portion of this amount included in the 1999-2001 executive budget:)**
- b. For the 1999-2001 biennium: \_\_\_\_\_  
**(Indicate the portion of this amount included in the 1999-2001 executive budget:)**
- c. For the 2001-03 biennium: \_\_\_\_\_

4. **County, city, and school district fiscal effect in dollar amounts:**

1997-99 Biennium			1999-2001 Biennium			2001-03 Biennium		
Counties	Cities	School Districts	Counties	Cities	School Districts	Counties	Cities	School Districts

If additional space is needed  
attach a supplemental sheet.

Signed: *Kathryn L. Strombeck*

Typed Name: Kathryn L. Strombeck

Department: Tax

Date Prepared: January 26, 1999

Phone Number: 328-3402

Please type or use black pen to complete

Date 2-8-99

Roll call vote # 1

### 1999 HOUSE STANDING COMMITTEE ROLL CALL VOTES

BILL/RESOLUTION NO. HB 1413

House HOUSE FINANCE & TAX Committee

Subcommittee on \_\_\_\_\_

Conference Committee

} Identify or check where appropriate

Legislative Council Amendment Number \_\_\_\_\_

Action Taken Do Not Pass

Motion Made By Rep. Grosz Seconded By Rep. Rennerfeldt

Representatives	Yes	No	Representatives	Yes	No
BELTER	✓		WINRICH		✓
RENNERFELDT	✓				
CLARK	✓				
FROELICH		✓			
GRANDE	✓				
GROSZ	✓				
HERBEL	✓				
KROEBER	✓				
MICKELSON		✓			
NICHOLAS	A				
RENNER	✓				
SCHMIDT	✓				
WARNER		✓			
WIKENHEISER	✓				

Total 10 4  
(Yes) (No)

Absent 1  
Floor Assignment Rep. Rennerfeldt

If the vote is on an amendment, briefly indicate intent:

DO NOT USE HIGHLIGHTER ON ANY FORMS

REPORT OF STANDING COMMITTEE (410)  
February 8, 1999 3:31 p.m.

Module No: HR-25-2222  
Carrier: Rennerfeldt  
Insert LC: . Title: .

**REPORT OF STANDING COMMITTEE**

**HB 1413: Finance and Taxation Committee (Rep. Belter, Chairman)** recommends **DO NOT PASS** (10 YEAS, 4 NAYS, 1 ABSENT AND NOT VOTING). HB 1413 was placed on the Eleventh order on the calendar.

**1999 TESTIMONY**

**HB 1413**



From: Randy Brown@rmb on 01/26/99 01:59 PM  
To: Jim A. Poolman/NDLC/NoDak@NoDak  
cc:  
Subject: HB 1413 Seed Capital Tax Credit

Jim, If you would rely this message to the Industry Business & Labor Committees I would appreciate it.

Representatives - As a business owner in the state of ND that employees over 200 people. I would like to express my opinion for the need of additional options business owners could possibly tap into to help establish or grow their ND businesses. The proposed HB 1413 Seed Capital Tax Credit bill could be a logical choice for both the business owner and the investor.

I don't think we have the luxury in this state to pass up opportunities that could help grow businesses and create more jobs. It's my personal opinion that this bill and other creative opportunities should be a must, we face many challenging times just to keep good business people and their employees in the state.

I make to you a strong recommendation as a business owner and investor to pass this bill

Thank you for your time

Randy Brown  
Pres. / CEO AGSCO, Grand Forks

1/27/99  
Herald EDITORIAL

Rush to

Rep. Jim Poolman

# Tax credit could groom hi-tech trail

Here's what they should do first: Change the name. Because in an age where thong underwear and the president of the United States get mentioned in the same breath, there's no way the "Seed Capital Tax Credit" proposal is going to get much press.

## OUR VIEW

Program would give taxpayers an incentive to invest in North Dakota firms.

But after that, the proposal's other details should be left alone. In fact they should become law. The tax credit may not sound sexy, but it's a farsighted idea that could help build innovation and entrepreneurialism in North Dakota. And that beats a recap of Bill's gifts to Monica any time.

The credit would work like this: If you invested, say, \$1,000 in a certified, North Dakota-based primary-sector company — basically, one whose product or service gets sold out-of-state — you could claim 30 percent of that investment as a tax credit. In this case, your North Dakota income tax bill would drop by \$300.

The company would get the capital, the investor would get the tax credit. But the state would profit, too. The "outside" dollars that these companies pull in "pay for new in-state jobs and generate new taxes that more than offset the tax credits," said Bruce Gjovig, director of the Center for Innovation and the Rural Technology Incubator at UND.

In return for the state assuming a small share of the risk, a large amount of investment cash could be kept in-state and directed toward those companies upon whom the state's future depends, Gjovig said. "This is good public policy."

And the state's liability is limited: The credit's impact on the treasury would be capped at \$250,000 a year.

The credit actually is available now. The catch is, you have to file North Dakota's "long form" to claim it. Less than 1 percent of North Dakota taxpayers use that form — so since 1993, when the credit was made available, not one taxpayer has claimed it, Gjovig said.

This afternoon, a House committee will hear a bill, sponsored by Rep. Jim Poolman of Grand Forks, that would let the credit be used on the "short form." The change makes sense. North Dakota needs to support its entrepreneurial start-ups more vigorously. By letting all taxpayers take advantage of the credit, the state would help stanch the flow of investment dollars, which currently pour out of state.

Those dollars are the fertilizer that "Dakota Made" products need. And keeping them on the prairie is the way to help those products grow.

— Tom Dennis for the Herald

Joseph Becker  
HB 1413

## Seed Capital Investment Income Tax Credit

- Statute: N.D.C.C. Chapter 57-38.5
- Administrative Rules: N.D. Admin. Code Section 81-03-02.1-12 and N.D. Admin. Code Section 81-03-01.1-08
- History: Created in 1993 (S.L. 1993, Chapter 560); amended in 1997 (S.L. 1997, Chapter 495)

### Overview

These provisions provide for a nonrefundable income tax credit for investing in a business certified as a qualified business for purposes of the seed capital investment credit. The credit is allowed to an individual, estate or trust.

### Definition of qualified business

A qualified business:

1. Is a for-profit corporation, partnership, limited partnership, limited liability company, limited liability partnership, joint venture, or has a satellite operation in North Dakota that is a for-profit corporation;
2. Is a primary sector business;
3. Satisfies the North Dakota securities filing requirements;
4. Either:
  - a. Maintains its principal office in North Dakota and, except for sales activity, conducts the majority of its business activity in North Dakota; or,
  - b. Maintains a significant operation in North Dakota having (or projected to have) more than 25 employees or annual sales of \$250,000;
5. Hires North Dakota resident individuals to fill the majority of its employment positions in either its principal office in North Dakota or its satellite operation in North Dakota;
6. Is owned by one or more individuals who hold the majority interest in the business and are involved in the business on a full-time basis; and,
7. Is certified by the Director of the Department of Economic Development and Finance to have met criteria 1 through 6 above.

### Who is eligible for credit?

The credit is allowed to the following:

1. Individual on Form 37 (Long Form, and
2. Estate or trust on Form 38 (Long Method).

**Exception for short form filer.** An individual electing to use Form 37-S (Short Form), or a fiduciary for an estate or trust electing to use the Short Method on Form 38, is ineligible for the tax credit for the taxable year of the election and for any subsequent taxable year to which the tax credit would otherwise be allowed as a carryover.

**Partnership.** If a partnership makes an investment, the tax credit must be determined at the partnership level, and the amount of the credit allowed at the partnership level is allowed to the partners (limited to individuals, estates and trusts) based on their respective interests in the partnership.

**Exception for majority owners.** An individual, estate or trust owning over 50% of the voting stock and over 50% of each class of other stock in an otherwise qualified business is not eligible for the credit. This ineligibility extends to the ineligible individual's spouse, parents, sibling, or child, and to the spouse of a sibling or child.

### **Amount of credit**

The amount of the credit allowed to a taxpayer is 30% of the investments in qualified businesses, subject to the following:

1. A minimum of \$5,000 must be invested during the taxpayer's taxable year,
2. The credit is limited to the first \$50,000 invested during the taxpayer's taxable year,
3. The allowable credit is first allowed and must be taken in the taxable year in which the investment is paid in full, but no more than 50% of the allowable credit may be used in the taxable year of the investment,
4. The allowable credit may only offset up to 50% of the taxpayer's tax liability in any taxable year, and
5. An unused credit may be carried forward 15 years.

### **Annual limitations on credit**

There are annual limitations on credits for investments by all taxpayers in one qualified business and in all qualified businesses.

1. Total credits allowed annually for investments by *all taxpayers in a particular qualified business* is limited to the lesser of:
  1. 30% of the investments in the qualified business,
  2. Gross receipts from out-of-state sales of the qualified business, or
  3. \$250,000.
2. Total credits allowed annually for investments by all taxpayers in all qualified businesses is \$250,000.
3. The annual limitations in items 1 and 2 above are measured on a calendar year basis.
4. If investments exceed the annual limits, the tax credits (limited to \$250,000) must be allowed to investors in the chronological order of their investments, as determined by the investment reporting forms filed with the Office of State Tax Commissioner (see attached).
  - a. For each qualifying investment, the qualified business must complete an investment reporting form.
  - b. Two copies must be given to the investor, one to be filed with the investor's North Dakota tax return and one for the investor's records.
  - c. One copy must be filed by the qualified business with the Office of State Tax Commissioner.

# Investment Reporting Form

## Seed capital investment credit (North Dakota Century Code ch. 57-38.5)

### General Information

This form facilitates the administration of the tax credit allowed under N.D.C.C. ch. 57-38.5 for investing in a business that has been certified by the Director of the Department of Economic Development and Finance as a qualified business for purposes of the credit. An authorized representative of the qualified business must complete and file this form with the Office of State Tax Commissioner within thirty days of the date on which full payment for the investment is received by the qualified business.

Two copies of the completed form must be given to the investor — one to be attached to the investor's tax return and one for the investor's files — and one copy should be retained by the qualified business for its files.

### Tax Credit Information

The tax credit is allowed to:

- An individual (on Form 37 only)
- An estate or trust (on Form 38, Long Method only)

An individual electing to use Form 37-S, or an estate or trust electing to use the Short Method on Form 38, is not eligible for the tax credit for the taxable year for which the election is made and any subsequent taxable year to which an unused tax credit could have been carried. An individual, estate, or trust owning a controlling interest in the qualified business, or an individual whose full-time professional activity is the operation of the qualified business, is not eligible for the tax credit. A spouse, parent, sibling, or child (or the spouse

of a sibling or child) of an ineligible individual is also ineligible for the tax credit.

If a partnership makes a qualifying investment, the amount of the tax credit must be determined at the partnership level as if the partnership were one taxpayer and must be allocated to the partners — limited to individuals, estates and trust — in proportion to their respective partnership interests. If a partnership and a partner have different taxable years, the amount of the tax credit allocated to the partner must be claimed in the partner's taxable year in which the partnership's taxable year ends.

The tax credit is equal to thirty percent of the amount invested, subject to the following:

- The tax credit is allowed only for investments totalling at least \$5,000 but no more than \$50,000 in a taxable year;
- The tax credit must be claimed first in the taxable year in which the investment is paid for in full, and only fifty percent of the total tax credit may be claimed in that first taxable year;
- Only fifty percent of the tax liability may be offset by the tax credit in any taxable year;
- The maximum amount of tax credits allowed to all taxpayers for investments made in the same qualified business during a calendar year period may not exceed the lesser of:
  1. Thirty percent of the investments,
  2. Gross receipts during the calendar year from out-of-state sales of the qualified business, or
  3. \$250,000.

The excess of tax credits over this maximum may not be claimed in any taxable year;

- The maximum amount of tax credits allowed to all taxpayers for investments made in all qualified businesses during a calendar year period may not exceed \$250,000. The excess of tax credits over this maximum may not be claimed in any taxable year; and
- If the tax credit exceeds the tax liability for the taxable year in which the tax credit is first allowed, the excess tax credit may be carried forward for up to fifteen taxable years.

If total tax credits exceed either of the calendar year limitations, the tax credits up to the amount of the limitation are allowed to taxpayers in the chronological order of their investments, as determined from the investment reporting forms filed by qualified businesses with the Office of State Tax Commissioner.

### For assistance call:

(701)328-3450

TDD/TTY users —  
(701)328-2778

1-800-453-8950 (toll free in North Dakota)

### Or write to:

Office of State Tax Commissioner  
State Capitol, 16th Floor  
600 E. Boulevard Ave.  
Bismarck, ND 58505-0599

### Investor information

Name of investor

Social security number (or Fed ID No)

Address of investor

City

State

Zip code

Date on which full payment for investment was received

Dollar amount paid for investment  
\$

### Qualified seed capital business information

Name of qualified seed capital business

Federal identification number

Address of qualified seed capital business

City

State

Zip code

Name of authorized representative (print)

Title

Signature

Date

TESTIMONY BEFORE FINANCE & TAXATION COMMITTEE  
JANUARY 27, 1999

Thank you Mr. Chairman and members of the committee.

I am here in support of HB 1413.

My name is Vivian Gwin and I am treasurer of Dakota Aero Manufacturers, a company that opened its doors in Devils Lake in July of last year. I can say without reservation that, without the tort reform legislation passed by this body in 1995 which sought to provide liability protection for the aviation industry, Dakota Aero would not be in existence today.

Our company will modify a line of twin-engine aircraft called Aero Commanders by completely rebuilding them and installing a newly certified engine that will improve their performance while reducing their operating cost. These are airplanes that will sell for \$1.2 to \$1.5 million, so you can imagine it took a substantial investment to get this business started.

In 1993 this body passed legislation that provided for seed capital tax credits for investment in primary sector ND businesses. What a wonderful idea--a way to encourage people to invest in North Dakota and create opportunities for economic development! But it was an idea that overlooked one small item--this tax credit could

only be used when filing long form—and how many folks file long form these days? I understand that, to date, not one single person has taken advantage of this tax credit.

Dakota Aero has had some experience in raising money—in 1995 we began the long and arduous task of assembling a group of qualified investors for an aviation project in ND. It took nearly 2 years, thousands of miles, and dozens of meetings to raise the necessary equity. And while we were successful in accomplishing this, our task would have been made much easier had this tax credit incentive been useable.

It appears we will be expanding in the near future and will have to, once again, raise a significant amount of equity capital. This expansion may create as many as 100 new high-paying jobs that will support an entire family and generate taxes for many years to come, as well as provide a very positive impact to the economy of Devils Lake and the state. Just think about the economic impact of 100 new jobs for this tax credit. The passage of HB 1413 will help make this growth a reality.

The 1995 tort reform legislation opened the door to a whole new industry in ND. This demonstrates that a piece of legislation can play a major role in affecting the economy of our state.

It is clearly in the best interest of North Dakota to continue to create an environment which fosters capital formation for primary sector industry. HB 1413 would play an important part in this effort. I urge you to support this legislation.

*Vivian Gwin 701-223-8363*



# Center for Innovation

P.O. Box 8372 • Grand Forks, North Dakota 58202-8372 • (701) 777-3132 • FAX (701) 777-2339

## In Support of: **HB 1413 Seed Capital Tax Credit**

Testimony from: Bruce Gjovig, Center for Innovation 777-3134 [gjovig@prairie.nodak.edu](mailto:gjovig@prairie.nodak.edu)

**Private Investment**, in particular seed capital, is needed to grow primary sector companies. Early financing is *very* difficult to secure for many companies developing a new product or technology, entering a new market, or in the early stages of rapid growth. Investment, especially private investment, is *essential* for growth that creates new products, wealth and jobs. North Dakota is a capital export state, with our citizens investing in distant capital markets fueling growth outside of North Dakota. To grow, we need to capture some of that investment at home.

Ten North Dakota growth companies were contacted about the seed capital tax credit. All said this could be a valuable tool in attracting investors. All said the current law was unusable in the current form, but raising capital is vital to their success. HB 1413 makes the tax credit useable.

The 1993 Legislature passed a 30% Seed Capital Tax Credit to encourage North Dakota investors to invest in growing primary sector companies in North Dakota. However the tax credit was only allowed on the long form when filing taxes. Since 1993 when the law was passed *not one taxpayer* has utilized the tax credit. So few taxpayers use the long form, that it renders the tax credit unusable. The tax credit needs to be on the "*short form*" for tax purposes to be effective.

In conversations with Tax Commissioner Rick Clayburgh, he indicated the change was workable to add one line to the "short form" for tax credits, attaching tax credit certificates in the amount of tax credits utilized, much like we attach W-2 forms. Economic Development Association of North Dakota (EDA-ND) is on record in support of HB 1413. Growing companies are very supportive, calling the seed capital tax credit change vital. Private investors need the incentive to invest in North Dakota. HB 1413 is vital, useable and workable.

### **Good Public Policy**

There are reasonable restrictions in the 1993 law (SB 2052 - Traynor) to ensure good public policy. The tax credit has a cap of \$250,000 per year, limiting the state's exposure to tax revenue losses. It is good public policy to encourage private investors to invest in North Dakota primary sector companies who sell products and services out-of-state. These "outside" dollars pay for new in-state jobs and **generate new taxes that more than offset the tax credits** because the leverage on the seed capital tax credit is greater than 1:9. The investor assumes the risk of the investment, does the due diligence, and completes all the paperwork. In other words, the taxpayer does all the work, and the state assumes a small share of the risk. This is cost-effective to administer, has high leverage, and encourages the private sector to do more in economic development - this is good public policy. HB 1413 is worthy of enthusiastic support.