



# House of Representatives

General Assembly

**File No. 496**

February Session, 2014

Substitute House Bill No. 5465

*House of Representatives, April 10, 2014*

The Committee on Finance, Revenue and Bonding reported through REP. WIDLITZ of the 98th Dist., Chairperson of the Committee on the part of the House, that the substitute bill ought to pass.

## ***AN ACT CONCERNING THE CONNECTICUT AEROSPACE REINVESTMENT ACT.***

Be it enacted by the Senate and House of Representatives in General Assembly convened:

1 Section 1. (NEW) (*Effective from passage*) (a) As used in this section:

2 (1) "Accumulated credits" means the amount of credits allowed, in  
3 accordance with the provisions of section 12-217n of the general  
4 statutes, that have not been taken through the last income year  
5 completed prior to the date of an application submitted as provided in  
6 subsection (b) of this section. The amount of such accumulated credits  
7 shall be subject to confirmation, in accordance with the provisions of  
8 title 12 of the general statutes, by the Commissioner of Revenue  
9 Services in consultation with the commissioner.

10 (2) "Base level" means the level set forth for each factor listed in  
11 subparagraph (A) of subdivision (6) of subsection (c) of this section, in  
12 the reinvestment contract for the most recently completed calendar

13 year prior to the designation as a state-certified industrial reinvestment  
14 project.

15 (3) "Commissioner" means the Commissioner of Economic and  
16 Community Development.

17 (4) "Eligible expenditures" means those expenditures made or  
18 incurred in this state by an eligible taxpayer in furtherance of a state-  
19 certified industrial reinvestment project, including, but not limited to,  
20 (A) expenditures with respect to buildings, improvements, property,  
21 plants and equipment, and expenses directly related to such  
22 expenditures, such as design work, professional fees, surveys and site  
23 preparation, remediation and clean-up, demolition, moving and  
24 renovation expenses, (B) expenditures with respect to personal  
25 property, (C) research and development expenses, as defined in  
26 section 12-217n of the general statutes, and (D) the hiring and training  
27 of employees.

28 (5) "Eligible taxpayer" means a taxpayer, or a group of taxpayers  
29 filing a combined return under section 12-223a of the general statutes,  
30 that, at the time application is made under subsection (b) of this  
31 section, (A) is primarily engaged in the industrial sector, (B) employs  
32 at least fifteen thousand people in the state, (C) has incurred at least  
33 two hundred million dollars per year in research and development  
34 expenses, as defined in section 12-217n of the general statutes, in the  
35 state for the five full income years immediately preceding the date of  
36 such application, and (D) has at least four hundred million dollars of  
37 accumulated credits.

38 (6) "Exchange year" means the period beginning on the date set  
39 forth in the reinvestment contract and ending on June 30, 2015, and  
40 each successive period ending on June thirtieth thereafter.

41 (7) "Income year" means the income year of an eligible taxpayer as  
42 determined under subsection (a) of section 12-213 of the general  
43 statutes.

44 (8) "Industrial reinvestment project" means one or more projects in  
45 this state that, if certified by the commissioner as provided in  
46 subsection (b) of this section, will entail aggregate eligible  
47 expenditures in the state of not less than one hundred million dollars  
48 over a period of not more than five exchange years by an eligible  
49 taxpayer in furtherance of the industrial reinvestment project. If an  
50 industrial reinvestment project is comprised of more than one project,  
51 each such project shall be referred to as a segment. Such segments shall  
52 be specifically set forth in the reinvestment contract.

53 (9) "Industrial sector" means all activities that, in accordance with  
54 the North American Industrial Classification System, United States  
55 Manual, United States Office of Management and Budget, 2012 edition,  
56 are included in Section 31, 32 or 33, including all operations in support  
57 of such activities.

58 (10) "Payment year" means the twelve-month period beginning on  
59 the date payments commence under the reinvestment contract and  
60 each twelve-month period thereafter.

61 (11) "Reinvestment contract" means a contract entered into between  
62 the commissioner and an eligible taxpayer in accordance with  
63 subsection (c) of this section.

64 (12) "State-certified industrial reinvestment project" means an  
65 industrial reinvestment project certified by the commissioner as  
66 provided in subsection (b) of this section.

67 (b) (1) Any eligible taxpayer that intends to undertake an industrial  
68 reinvestment project may apply to the commissioner for certification of  
69 such project as a state-certified industrial reinvestment project. In  
70 order to receive such certification, an eligible taxpayer shall apply to  
71 the commissioner, in a form acceptable to the commissioner and  
72 containing such information as prescribed by the commissioner,  
73 including, but not limited to, a detailed plan outlining the industrial  
74 reinvestment project, the term of such project, the estimated costs of  
75 such project and the amount of accumulated credits the eligible

76 taxpayer proposes it be allowed to exchange in connection with such  
77 project. The commissioner may require the eligible taxpayer to submit  
78 such additional information as may be necessary to evaluate the  
79 application.

80 (2) All decisions of the commissioner with respect to applications  
81 received under the provisions of subdivision (1) of this subsection shall  
82 be at the commissioner's sole discretion. The provisions of this  
83 subsection shall not be construed as authorizing suit against the state  
84 by any taxpayer that is denied certification by the commissioner and  
85 shall not be construed as a waiver of sovereign immunity.

86 (c) (1) Upon certification by the commissioner of an application as  
87 provided in subsection (b) of this section, the commissioner may enter  
88 into a reinvestment contract with an eligible taxpayer pursuant to  
89 which the commissioner may, in consideration of the eligible  
90 taxpayer's agreement to make the eligible expenditures in connection  
91 with the state-certified industrial reinvestment project, agree to  
92 exchange certain of the eligible taxpayer's accumulated credits up to a  
93 specified amount. Such reinvestment contract shall specify (A) the  
94 length of time the state-certified industrial reinvestment project will  
95 take to complete, (B) the aggregate amount of eligible expenditures the  
96 eligible taxpayer agrees to make, (C) the amounts, as determined in  
97 accordance with the provisions of subdivision (6) of this subsection,  
98 that the eligible taxpayer is entitled to receive during the term of such  
99 reinvestment contract with respect to such eligible expenditures, and  
100 the terms and conditions the eligible taxpayer must satisfy in order to  
101 receive such amounts, (D) the terms and conditions of the repayment  
102 of any such amounts paid to the eligible taxpayer in exchange for the  
103 accumulated credits in the event of any failure on the part of the  
104 eligible taxpayer to comply with the terms of the reinvestment  
105 contract, and (E) any other terms and conditions the commissioner  
106 may require. Any eligible taxpayer that enters into a reinvestment  
107 contract with the commissioner under this subsection may, in the  
108 event of any disputed claims under such reinvestment contract, bring  
109 an action against the state to the superior court for the judicial district

110 of Hartford for the purpose of having such claim determined,  
111 provided notice of any such disputed claim is first given to the  
112 commissioner in the method and manner prescribed by such  
113 reinvestment contract. No action shall be allowed unless it is brought  
114 not later than two years after the date on which the eligible taxpayer  
115 gave proper notice to the commissioner under such reinvestment  
116 contract. All legal defenses, except sovereign immunity, are reserved  
117 to the state.

118 (2) The payment by the state of amounts directly attributable to the  
119 exchange of accumulated credits in connection with a state-certified  
120 industrial reinvestment project may be made in the form, timing and  
121 manner determined by the commissioner, including as an offset or  
122 refund of state taxes otherwise payable by the eligible taxpayer under  
123 the provisions of chapters 208 and 219 of the general statutes. To the  
124 extent that such payments involve the offset or refund of state taxes,  
125 such payments shall be made in consultation with the Commissioner  
126 of Revenue Services.

127 (3) The provisions of subsection (d) of section 12-217n of the general  
128 statutes, sections 12-217aa and 12-217zz of the general statutes,  
129 subsections (c) and (e) of section 32-223 of the general statutes, and  
130 section 32-462 of the general statutes, shall not apply to a reinvestment  
131 contract to the extent such provisions are inconsistent with such  
132 reinvestment contract.

133 (4) Subject to the provisions of subdivision (5) of this subsection, the  
134 amount of accumulated credits that an eligible taxpayer is allowed to  
135 exchange with respect to any state-certified industrial reinvestment  
136 project shall not exceed the eligible expenditures made by such  
137 taxpayer with respect to such project. No eligible taxpayer shall make  
138 any further claims with respect to any accumulated credits exchanged  
139 in connection with a state-certified industrial reinvestment project. The  
140 commissioner shall notify the Commissioner of Revenue Services of all  
141 accumulated credits, and the amounts thereof, exchanged in  
142 connection with such project.

143 (5) The aggregate amount of all payments made by the state under  
 144 this section for the exchange of accumulated credits shall not exceed  
 145 four hundred million dollars, provided (A) the amount of all payments  
 146 made by the state during any of the first five payment years shall not  
 147 exceed twenty million dollars per year, and (B) the amount of all  
 148 payments made by the state during any of the sixth or subsequent  
 149 payment years shall not exceed the sum of thirty-three million three  
 150 hundred thirty-four thousand dollars per year.

151 (6) Subject to the provisions of subdivisions (4) and (5) of this  
 152 subsection, the amounts an eligible taxpayer is entitled to receive  
 153 under a reinvestment contract with respect to eligible expenditures  
 154 made by such taxpayer shall be determined in accordance with  
 155 subparagraph (A) or (B) of this subdivision.

156 (A) (i) If, in connection with a state-certified industrial reinvestment  
 157 project, or segment thereof, an eligible taxpayer may qualify to receive  
 158 more than two hundred million dollars upon compliance with the  
 159 terms of the reinvestment contract, the amount the eligible taxpayer is  
 160 eligible to receive with respect to such project or segment shall be  
 161 determined by multiplying the actual amount of eligible expenditures  
 162 made in each of the first five exchange years by the total of the four  
 163 applicable weighting factors as determined in accordance with  
 164 subparagraphs (A)(i)(I) to (A)(i)(IV), inclusive, of this subdivision.

165 (I) The weighting factor for the maintenance or increase of  
 166 employment levels of engineers located in this state shall be calculated  
 167 in accordance with the following table:

T1	Employment Levels of Engineers	Weighting Factors
T2	(Individuals Employed)	
T3	Below 4,350	0%
T4	4,350	7%
T5	4,400	8%
T6	4,450	9%
T7	4,500	10%
T8	4,550	11%
T9	4,600	12%

T10	4,650	13%
T11	4,700	14%
T12	4,750	15%
T13	4,800	16%
T14	4,850	17%
T15	4,900 (Base Level)	18%
T16	4,950	19%
T17	5,000	20%

168 The base level for the weighting factor for employment levels of  
 169 engineers located in this state is four thousand nine hundred  
 170 employees. The actual percentage for such factor shall be interpolated  
 171 in accordance with this table.

172 (II) The weighting factor for the maintenance or increase of overall  
 173 employment levels in this state shall be calculated in accordance with  
 174 the following table:

T18	Overall Employment Levels	Weighting Factors
T19	(Individuals Employed)	
T20	Below 12,450	0%
T21	12,450	10.5%
T22	12,600	12%
T23	12,750	13.5%
T24	12,900	15%
T25	13,050	16.5%
T26	13,200	18%
T27	13,350	19.5%
T28	13,500	21%
T29	13,650	22.5%
T30	13,800	24%
T31	13,950	25.5%
T32	14,100 (Base Level)	27%
T33	14,250	28.5%
T34	14,400	30%

175 The base level for the weighting factor for overall employment levels  
 176 in this state is fourteen thousand one hundred employees. The actual  
 177 percentage for this factor shall be interpolated in accordance with this  
 178 table.

179 (III) The weighting factor for the maintenance or increase of payroll  
180 levels in this state shall be calculated in accordance with the following  
181 table:

T35	Payroll Levels	Weighting Factors
T36	Below \$1,370,000,000	0%
T37	1,370,000,000	0.5%
T38	1,385,000,000	12%
T39	1,400,000,000	13.5%
T40	1,415,000,000	15%
T41	1,430,000,000	16.5%
T42	1,445,000,000	18%
T43	1,460,000,000	19.5%
T44	1,475,000,000	21%
T45	1,490,000,000	22.5%
T46	1,505,000,000	24%
T47	1,520,000,000	25.5%
T48	1,535,000,000 (Base Level)	27%
T49	1,550,000,000	28.5%
T50	1,565,000,000	30%

182 The base level for the weighting factor for the payroll levels in this  
183 state is one billion five hundred thirty-five million dollars. The actual  
184 percentage for this factor shall be interpolated in accordance with this  
185 table.

186 (IV) The weighting factor for research and development expenses  
187 and capital expenditures, exclusive of those eligible expenditures made  
188 in accordance with a contract entered into with the commissioner  
189 under the provisions of this subsection, shall be calculated in  
190 accordance with the following table:

T51	Investment Amount	Weighting Factors
T52	Below \$680,000,000	0%
T53	680,000,000	7%
T54	690,000,000	8%
T55	700,000,000	9%
T56	710,000,000	10%
T57	720,000,000	11%
T58	730,000,000	12%

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T59	740,000,000	13%
T60	750,000,000	14%
T61	760,000,000	15%
T62	770,000,000	16%
T63	780,000,000	17%
T64	790,000,000 (Base Level)	18%
T65	800,000,000	19%
T66	810,000,000	20%

191 The base level for the weighting factor for research and development  
192 expenses and capital expenditures in this state, exclusive of such  
193 eligible expenditures made in connection with the reinvestment  
194 contract, is seven hundred ninety million dollars. The actual  
195 percentage for this factor shall be interpolated in accordance with this  
196 table.

197 (ii) The eligible taxpayer shall certify the base levels set forth in  
198 subparagraphs (A)(i)(I) to (A)(i)(IV), inclusive, of this subdivision to  
199 the commissioner, and shall do so not later than one hundred twenty  
200 days after entering into a reinvestment contract with the  
201 commissioner. In the event any of the base levels certified to the  
202 commissioner differ from those set forth in said subparagraphs, the  
203 commissioner is authorized to adjust the base levels and recalculate  
204 the tables for the weighting factors consistent with subparagraphs  
205 (A)(i)(I) to (A)(i)(IV), inclusive, of this subdivision.

206 (iii) The aggregate amount of all payments made by the state under  
207 this subparagraph for the exchange of accumulated credits shall not  
208 exceed three hundred seventy-five million dollars.

209 (B) If, in connection with a state-certified industrial reinvestment  
210 project, or segment thereof, an eligible taxpayer may receive fifty  
211 million dollars or less upon compliance with the terms of the  
212 reinvestment contract, the amount the eligible taxpayer is eligible to  
213 receive with respect to such project or segment shall be determined  
214 with reference to the performance of the eligible taxpayer during the  
215 first five exchange years and shall be calculated as follows: (i) To the  
216 extent that expenditures by the eligible taxpayer with respect to one or

217 more research and development components of such project or  
218 segment involve over ten million dollars in research and development  
219 expenses and involve the retention of one hundred or more employees,  
220 the eligible taxpayer is eligible to receive one million dollars with  
221 respect to each such component; and (ii) to the extent that expenditures  
222 by the eligible taxpayer with respect to one or more capital  
223 components of such project or segment involve over one million  
224 dollars in capital expenditures, the eligible taxpayer is eligible to  
225 receive forty per cent of such expenditures with respect to each such  
226 component. The aggregate amount of all payments made by the state  
227 under this subparagraph for the exchange of accumulated credits shall  
228 not exceed fifty million dollars.

229 (d) Notwithstanding any provision of the general statutes, an  
230 eligible taxpayer that enters into a reinvestment contract with the  
231 commissioner under the provisions of this section and is authorized to  
232 exchange accumulated credits in connection with a state-certified  
233 industrial reinvestment project shall not be allowed any credit  
234 pursuant to section 12-217j or 12-217n of the general statutes, during  
235 the exclusion period under such reinvestment contract, or be eligible to  
236 exchange credits under the provisions of section 12-217ee of the  
237 general statutes, during such exclusion period. For purposes of this  
238 subsection, the exclusion period means those income years of the  
239 eligible taxpayer specified by the commissioner in the reinvestment  
240 contract as comprising the exclusion period. This subsection shall not  
241 preclude an eligible taxpayer (1) from taking accumulated credits that  
242 are not otherwise subject to exchange pursuant to such reinvestment  
243 contract during such exclusion period as otherwise allowed by law, or  
244 (2) from taking credits allowed under section 12-217j of the general  
245 statutes during the exclusion period as otherwise allowed by law.  
246 Except as provided herein, this subsection shall not impact an eligible  
247 taxpayer's ability to claim those tax credits it has already been allowed  
248 or otherwise affect such taxpayer's eligibility for credits under the  
249 provisions of the general statutes.

250 (e) To provide incentives for the retention and creation of jobs and

251 business growth in the state, the commissioner shall analyze and, as  
252 appropriate, seek additional legislative approval for programs  
253 permitting eligible taxpayers to exchange any accumulated credits in  
254 manners not otherwise provided for under this section.

255 (f) The commissioner shall include in the report required pursuant  
256 to section 32-1m of the general statutes an annual report that shall  
257 include information on the number of projects certified under this  
258 section, the number of reinvestment contracts entered into in  
259 connection with such projects, the status of the certified projects, the  
260 amount of accumulated credits that have been exchanged in  
261 connection with such projects, and the specific levels achieved by each  
262 eligible taxpayer under subparagraphs (A) and (B) of subdivision (6) of  
263 subsection (c) of this section.

264 (g) On and after December 31, 2019, the commissioner shall not  
265 certify any industrial reinvestment projects under subsection (b) of this  
266 section or enter into any reinvestment contracts under subsection (c) of  
267 this section.

This act shall take effect as follows and shall amend the following sections:		
Section 1	<i>from passage</i>	New section

**FIN** Joint Favorable Subst.

The following Fiscal Impact Statement and Bill Analysis are prepared for the benefit of the members of the General Assembly, solely for purposes of information, summarization and explanation and do not represent the intent of the General Assembly or either chamber thereof for any purpose. In general, fiscal impacts are based upon a variety of informational sources, including the analyst's professional knowledge. Whenever applicable, agency data is consulted as part of the analysis, however final products do not necessarily reflect an assessment from any specific department.

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### **OFA Fiscal Note**

#### **State Impact:**

<b>Agency Affected</b>	<b>Fund-Effect</b>	<b>FY 15 \$</b>	<b>FY 16 \$</b>
Department of Revenue Services	GF - Revenue Loss	Uncertain	Up to 20 Million

#### **Municipal Impact:**

<b>Municipalities</b>	<b>Effect</b>	<b>FY 15 \$</b>	<b>FY 16 \$</b>
East Hartford; Windsor Locks	Grand List Expansion	None	Potential

#### **Explanation**

The bill establishes a new tax credit exchange program available to certain manufacturers. In particular, the bill enables a tentative agreement between the state and United Technologies Corporation (UTC). That tentative agreement, as reported, involves the exchange of \$400 million over 14 years. These exchanges would reduce state revenue accordingly.

The bill authorizes the Commissioner of the Department of Economic and Community Development (DECD) to enter into contracts with eligible taxpayers to exchange accumulated Research and Development tax credits in amounts that are equal to eligible expenditures by the taxpayer in furtherance of an industrial reinvestment project. The bill establishes six factors that the Commissioner must use to determine the amounts (within the totals allowed by the bill) exchanged in any given year.

The bill limits the aggregate amount of tax credits that can be exchanged under the program to \$400 million. The bill also limits the

annual amounts that may be exchanged to \$20 million in each of the first five payment years of an agreement and \$33.3 million in the sixth and each subsequent year of a contract. The amounts to be exchanged may be less in any given year based on the extent to which the eligible taxpayer achieves the targets set forth in the bill and ultimately the contract.

Although the bill grants the Commissioner of the DECD discretion in determining the form, timing and manner of payments to UTC, it is anticipated that no payments would occur prior to FY 16 because payments are made according to eligible expenditures within exchange years, as defined by the bill. The first exchange year ends June 30, 2015. It is anticipated that it would take up to four months after the exchange year ends to certify eligible expenditures and process payments. Therefore, the first annual revenue loss is expected to occur in FY 16.

## **BACKGROUND**

### **Program Summary**

The bill establishes a program to allow the Commissioner of DECD to compensate eligible taxpayers for certain expenditures related to undertaking large-scale industrial reinvestment projects. Compensation would be made through an offset or refund of state taxes otherwise payable by the eligible taxpayer.

Eligible taxpayers must meet the following criteria: 1) be primarily engaged in the manufacturing sector; 2) employ at least 15,000 people in the state; 3) have incurred at least \$200 million per year in research and development expenses in the state for the five full income years immediately preceding the date of application; and 4) have at least \$400 million of accumulated research and development tax credits.

Eligible expenditures subject to state reimbursement include: 1) buildings, improvements, property, plants and equipment, and expenses directly related to such expenditures; 2) personal property; 3)

research and development expenses; and 4) hiring and training of employees.

Compensation will be made pursuant to contracts entered into between the Commissioner of DECD and eligible taxpayers. Pursuant to the bill, any such contract shall include an exclusionary period during which the eligible taxpayer is not allowed to earn additional Research and Development tax credits.

### **Current Status**

According to public reports, UTC would be eligible to participate in the bill's program and intends to apply to participate in it, subject to a tentative agreement reached between UTC and the Office of Policy and Management (OPM) / DECD. The tentative agreement would require a capital investment of approximately \$500 million by UTC in this state over the next five years.

Pursuant to the tentative agreement, UTC would receive up to \$400 million over 14 years in tax offsets or refunds drawn from its accumulated research and development tax credits, provided that: 1) DECD approves at least that amount as eligible expenditures pursuant to the bill; and 2) UTC meets or exceeds specified staffing, research and development and capital expenditure targets. The tentative agreement includes the construction of new facilities in East Hartford and a renovated facility in Windsor Locks.

### **Municipal Impact**

Encouraging industrial development in East Hartford and Windsor Locks will expand the taxable grand lists of those two towns, which will result in an increased levy in each, given a constant mill rate.

The grand list increase in each town depends on the assessed value of each project, when each project begins, and when each is completed. As towns assess the value of properties under construction, it is anticipated that the grand list increase in each town would be phased in over the duration of construction.

It is not known what the assessed value of the new facilities will be, during or after construction. However, the assessed value of UTC land on the 2011 Grand List is approximately \$319.1 million in East Hartford and \$39.1 million in Windsor Locks. Below is a table that shows the additional levy to each town, given a range of assumptions concerning the percent increase in the assessed value of UTC land. Tax payments are calculated using FY 14 mill rates of 43.9 for East Hartford and 24.54 for Windsor Locks.

<b>Changes to the Assessed Value of UTC land and its Impact on UTC Property Tax Payments in East Hartford and Windsor Locks</b>		
<b>% Increase in Assessed Value</b>	<b>East Hartford Additional Tax Payment (\$)</b>	<b>Windsor Locks Additional Tax Payment (\$)</b>
0.05	700,387	47,930
0.10	1,400,774	95,860
0.15	2,101,162	143,789
0.20	2,801,549	191,719
0.25	3,501,936	239,649

To the extent that this bill encourages additional development in East Hartford, Windsor Locks, or other towns, there would be an additional expansion to their grand lists. Any expansion would result in an increase in tax levy, given a constant mill rate.

### ***The Out Years***

#### ***State Impact:***

The bill limits the annual state revenue loss under any agreement to \$20 million in the first five years (\$100 million total) and \$33.3 million in each of the subsequent nine fiscal years (\$300 million total).

The value of the taxable grand list expansions triggered by the bill for East Hartford and Windsor Locks would grow subject to inflation.

*Sources: Public Hearing Testimony*

**OLR Bill Analysis****sHB 5465*****AN ACT CONCERNING THE CONNECTICUT AEROSPACE REINVESTMENT ACT.*****SUMMARY:**

This bill creates a program that compensates large manufacturers proposing industrial reinvestment projects (IRP) for unused state research and development (R&D) tax credits. A manufacturer qualifies for compensation if it meets specified criteria and agrees to spend at least \$100 million over five years on an IRP, which may consist of activities ranging from constructing new plants to hiring and training employees.

The bill authorizes the Department of Economic and Community Development (DECD) commissioner to run the program, specifying the process she must use to (1) certify if manufacturers and their proposed IRPs meet the bill's criteria and (2) enter into contracts providing compensation payments for credits in exchange for undertaking an IRP. The commissioner's authority to certify IRPs or enter into reinvestment contracts ends December 31, 2019.

The bill also authorizes the commissioner to determine the amount of unused credits eligible for compensation and specifies the methods she must use to calculate the credit compensation payments. The methods vary depending on an IRP's total eligible expenditures plus the degree to which certain weighted performance factors fall above or below the bill's base levels for each factor.

The bill imposes program, annual, and project payment caps and prohibits manufacturers approved for payments from earning new R&D credits or exchanging them for cash, as the law currently allows.

The bill requires the commissioner to (1) identify other credit exchange options that could help manufacturers (a) grow and (b) create or retain jobs here and (2) as appropriate, propose legislation authorizing these options.

Lastly, the bill requires the commissioner to report on approved IRPs in her comprehensive annual report to the governor and legislature.

EFFECTIVE DATE: Upon passage

### **ELIGIBLE MANUFACTURERS**

The bill allows manufacturers to exchange accumulated state R&D tax credits for credit exchange payments if DECD certifies their proposed IRP and enters into a reinvestment contract with them, as described below. A manufacturer, or a group of manufacturers filing a combined corporation tax return, qualifies for these payments if it:

1. engages in an industrial sector activity, as defined in the federal Office of Management and Budget's *North American Industrial Classification System*, 2012 edition (industrial sectors 31, 32, or 33);
2. employs at least 15,000 people in Connecticut;
3. spent at least \$200 million per year on federally tax deductible R&D in Connecticut during the five full income years immediately before proposing an IRP for certification (see below); and
4. has at least \$400 million in accumulated state R&D credits.

### **ELIGIBLE IRPs**

To qualify for credit exchange payments, an eligible manufacturer must propose an IRP that meets the bill's criteria. Through the IRP the manufacturer must incur at least \$100 million in eligible expenditures in Connecticut for:

1. buildings, improvements, property, plants, and equipment

- (physical development);
2. design work, professional fees, surveys and site preparation, remediation and cleanup, demolition, moving and renovation expenses, and other activities directly related to the physical development activities;
  3. personal property;
  4. federally tax-deductible R&D; and
  5. employee hiring and training.

The manufacturer must incur these IRP-eligible expenditures within five “exchange years,” the period during which it is eligible for credit exchange payments. Such years run from July 1 to June 30. The first year begins on the date specified in the contract between the manufacturer and DECD and ends on June 30, 2015.

### **IRP CERTIFICATION**

Manufacturers seeking credit exchange payments must propose an IRP and submit it to the DECD commissioner, who must certify that it meets the bill’s criteria. A manufacturer must submit the request for certification on a form acceptable to the commissioner containing the information she requires. At a minimum, the manufacturer must:

1. provide a detailed plan outlining the IRP,
2. indicate how long it will take to complete it,
3. estimate the IRP’s costs, and
4. specify the amount of unused credits the taxpayer proposes to exchange for undertaking the IRP.

The commissioner may require any additional information she needs to evaluate the request. The bill specifies that the amount of unused credits she approves for the payments is subject to the revenue services commissioner’s confirmation.

The bill specifies that (1) only the DECD commissioner may decide whether to certify a proposed IRP and (2) the manufacturer cannot construe this authority as (a) a waiver of the state's sovereign immunity or (b) allowing it to sue the state if she denies certification.

## **REINVESTMENT CONTRACT**

### ***Content***

The bill's vehicle for the credit exchange payments is the reinvestment contract between the commissioner and the manufacturer. The contract, which the commissioner may execute after certifying the proposed IRP, must specify:

1. the deadline for completing the IRP;
2. the total amount of eligible expenditures the manufacturer agrees to make to complete it;
3. the amount of the credit exchange payment, determined by the bill's formula;
4. the terms and conditions the manufacturer must satisfy to receive these payments;
5. a requirement to repay the payments for failing to comply with the contract; and
6. any other terms and conditions the commissioner chooses to impose.

The bill exempts reinvestment contracts from the laws (1) limiting the extent to which credits can be used to reduce a business' tax liability, (2) specifying how R&D credits must be calculated, (3) listing the order in which credits for different purposes may be used, (4) limiting the amount of economic development funds a project may receive, and (5) requiring legislative approval for such projects when the amount of assistance exceeds specified amounts.

### ***Resolving Disputes***

If a manufacturer cannot resolve any claims under the contract, the bill allows it to sue the state in the Hartford Superior Court. The manufacturer must first notify the commissioner by providing such notice as the contract requires. It must also bring the action within two years of this notice. The bill reserves all legal defenses to the state except sovereign immunity.

## **CREDIT EXCHANGE PAYMENTS**

### ***Form of Compensation***

Manufacturers with unused R&D tax credits can exchange them for payments if they propose an IRP. The exchangeable credits may only include those a manufacturer accumulated up to the end of the last income year before it submitted an IRP for certification.

The commissioner may determine how and when she will make these payments, including their form and manner, which under the bill includes corporation business or sales and use tax refunds or offsets. Under current law, the commissioner provides grants, loans, loan guarantees, and other forms of financial assistance to businesses under various economic development programs. If she chooses to provide refunds or offsets under the bill, she must consult with the revenue services commissioner when providing them.

### ***Credit Exchange Payment Caps***

The bill specifies how the commissioner must calculate credit exchange payments, which are subject to program, annual, and project caps. The bill caps the total amount of payments under the program at \$400 million and further caps annual payments at (1) \$20 million per year during the first five years the state makes payments under a reinvestment contract and (2) \$33,334,000 per year for the sixth and subsequent payment years under that contract.

The bill also caps the total amount of accumulated credits a manufacturer can exchange under an IRP at the total amount of the project's eligible expenditures. As discussed below, the amount of these expenditures partly determines the amount of credit exchange

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payments a manufacturer may receive under a reinvestment contract.

The project caps vary depending on the total payment amount and the rules for calculating annual payments. The bill imposes a \$375 million cap on projects entitling a manufacturer to more than \$200 million in credit exchange payments for the entire project or a segment of it. It also imposes a \$50 million cap on projects entitling a manufacturer to \$50 million or less in credit exchange payments.

The bill bars a manufacturer from making any further use of those credits it exchanges for incurring the eligible expenditures. If the value of those credits is less than the total value of the manufacturer's accumulated credits, the bill implicitly allows the manufacturer to use the credits that are not part of the IRP as the law requires.

The DECD commissioner must notify the DRS commissioner of the value of the credits she approves for credit exchange payments under a reinvestment contract.

### ***Calculating Credit Exchange Payments—General***

The bill provides two methods for calculating credit exchange payments, depending on the total value of payments the DECD commissioner agrees to make in exchange for the manufacturer incurring eligible expenditures under the reinvestment contract. Consequently, it divides IRPs into two categories, each with different rules for calculating credit exchange payments. In both cases, the manufacturer receives the payments only if it complies with the reinvestment contract.

### ***Calculating Credit Exchange Payments for Large IRPs***

For IRPs entitling a manufacturer to over \$200 million in credit exchange payments for the entire project or a segment of it (up to the \$375 million cap mentioned above), the credit exchange payments in each of the first five payment years equals a portion of the eligible expenditures incurred during each of those five years.

The DECD commissioner must determine that portion by

multiplying the total eligible expenditures incurred during a year by the sum of four “weighting factors” expressed as percentages reflecting the degree to which the manufacturer’s actual (1) workforce and (2) R&D and capital expenditure levels in Connecticut fell above or below a specific benchmark or base level. The R&D and capital expenditure levels exclude expenditures incurred under a reinvestment contract. It appears that the R&D and capital expenditure levels include expenditures incurred outside the state.

Table 1 identifies the weighting factors, the maximum percentage weighting for each factor, the base level, and the range of weighting percentages for actual levels above or below that level.

**Table 1: Weighting Factors for Calculating Large IRP Credit Exchange Payments**

<b>Performance Factor Components</b>	<b>Performance Factors</b>			
	<b>Employment Level of Engineers in Connecticut</b>	<b>Overall Connecticut Employment Level</b>	<b>Connecticut Payroll Levels</b>	<b>R&amp;D and Capital Expenditure Levels</b>
Maximum Weighting Percentage	20%	30%	30%	20%
Base Level	4,900 engineers	14,100 employees	\$1.535 million	\$790.0 million
Range of Weighting Percentages	Below 4,350: 0% 4,900 base level: 18% 5,000: 20%	Below 12,450: 0% 14,100 base level: 27% 14,400: 30%	Below \$1.370 million: 0% \$1.535 million base level: 27% \$1.565 million: 30%	Below \$680.0 million: 0% \$790.0 million base level: 18% \$810.0 million: 20%

As noted above, the commissioner determines an annual credit exchange payment by multiplying the eligible expenditure for a payment year by the sum of the percentages for each weighting factor. For example, if a manufacturer incurred \$10 million in eligible expenditures, employed 5,000 engineers in Connecticut, employed 14,100 people here in all occupational categories (including the 5,000 engineers), spent \$1.535 million on payroll, and made \$810.0 million in R&D and capital expenditures, the annual credit exchange payment for

the manufacturer is \$9.4 million (\$10 million times 94%).

Under the bill, the manufacturer must certify the bill's base levels to the DECD commissioner within 120 days after executing the reinvestment contract. If the manufacturer certifies different levels, the commissioner may adjust the base levels and recalculate the weighting factors consistent with the bill format. (The bill does not prescribe a method for recalculating the weighting factors.)

### ***Calculating Credit Exchange Payments for Small IRPs***

The bill provides a separate method for calculating the credit exchange payments for IRPs entitling a manufacturer to \$50 million or less in such payments. It tacitly allows the manufacturer to divide an IRP or its segments into separate R&D and capital expenditures components and bases the payments on the total spending for (1) each capital component and (2) all R&D components, plus the number of employees the manufacturer retained in Connecticut during that payment year. (The bill does not specify how the commissioner must determine if the manufacturer meets this employee retention requirement.)

Table 2 shows the required spending and employment retention levels for each component type.

**Table 2: Schedule for Calculating Credit Exchange Payment for Small IRPs**

<b><i>Component Type</i></b>	<b><i>Minimum Requirement</i></b>	<b><i>Credit Exchange Payment Amount</i></b>
Capital Component	Over \$1 million per component	40% of the total expenditure for each component over \$1 million
R&D Component	Over \$10 million for all components and retain at least 100 employees in Connecticut	\$1 million per component

## **RESTRICTIONS ON EARNING NEW CREDITS OR EXCHANGING UNUSED CREDITS DURING EXCLUSION PERIOD**

The bill prohibits manufacturers approved for credit exchange payments from earning new R&D credits or exchanging them, as the law allows, for a refund equal to 65% of their value during the “exclusion period,” which the bill defines only as whatever period is specified in the reinvestment contract. This ban applies to the 20% incremental and rolling R&D credits (CGS § 12-217j and CGS § 12-217n, respectively) (See BACKGROUND).

The bill does not stop manufacturers approved for credit exchange payments from using, during the exclusion period, any (1) accumulated credits that are not being exchanged under a reinvestment contract or (2) incremental R&D credits. It does not stop them from using other already approved credits or affect their eligibility for them.

## **LEGISLATIVE REPORT**

The commissioner must report on the credit exchange payments in her comprehensive annual report to governor and legislature. In doing so, she must include the number of projects she approved and reinvestment contracts she executed, the status of each certified IRP, the amount of credits exchanged, and the performance levels the manufacturers achieved to obtain the payment amounts.

## **BACKGROUND**

### ***R&D Tax Credit***

The law authorizes two types of R&D tax credits against the state’s corporation tax. It authorizes a credit equal to 20% of the annual increase in R&D expenditures over the prior year (CGS § 12-217j) and a rolling credit based on a manufacturer’s size, location, and total annual R&D expenditures (CGS § 12-217n). Regarding the latter, the credit equals the greater of: (1) 3.5% of a manufacturer’s annual R&D expenditures or (2) the amount derived using a two-step formula for calculating credit amounts, whichever is greater. Applying the formula, the manufacturer first calculates the tentative credit amount, based on its total R&D expenditure for the year. The amount ranges from 1% of R&D expenditures totaling less than \$50 million to \$5.5

million plus 6% of R&D expenditures above \$200 million.

The second step limits the actual amount of credit the manufacturer may claim to the greater of the following amounts:

1. 50% of the tax liability without subtracting the R&D credit or
2. the lesser of (a) 200% of the total tentative credit amount, as determined in the first step, or (b) 90% of the total tax bill, without subtracting the R&D credit.

The credit for manufacturers that do not meet the location, size, and annual revenue criteria equals the amount derived from applying the two-step formula.

***Accumulating Unused R&D Tax Credits***

A manufacturer accumulates R&D credits as well as those for other purposes when the credit amounts exceed its tax liability or the credit (1) cannot be transferred or assigned to another taxpayer or (2) carried forward or backward for application against future or passed tax liability. Other factors that might cause a manufacturer to accumulate credits are the laws barring them from using credits to reduce their annual tax liability by more than 70% (CGS § 12-217zz) and specifying the order in which they may claim credits (CGS § 12-217aa).

**COMMITTEE ACTION**

Finance, Revenue and Bonding Committee

Joint Favorable Substitute  
Yea 50 Nay 0 (04/01/2014)