

**Testimony of
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Before the
Commerce Committee
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Good Afternoon. My name is Bonnie Stewart and I am Vice President of Government and Public Affairs & General Counsel for the Connecticut Business and Industry Association (CBIA). CBIA represents more than 10,000 job creators throughout the state of Connecticut ranging from one-person businesses to large corporations. The majority of our members have fewer than 25 employees.

Thank you for the opportunity to support and seek modifications to several measures before the committee today. However, in light of the Governor's recent spending and revenue proposals, I'd be remiss if I didn't first touch on the impact his proposal would have, both on the measures before you and on the state.

Although we recognize the difficult challenges facing the Governor and the legislature in closing budget deficits, we shouldn't close gaps by inhibiting investments by the very companies that drive our economy. The best way to grow revenues is to grow our economy. Yet in the Governor's proposal, key investment incentives and previously scheduled tax reductions were eliminated. This will strike a serious blow to business confidence in Connecticut as the economy continues to recover.

Repeatedly we hear from Connecticut's job creators that they need consistency and predictability when planning their investments. The research and development (R&D) cycle typically takes anywhere from five to 20 years (see enclosed chart). The manufacturing cycle for products developed through R&D ranges from five to more than 30 years. If the state of Connecticut wants these types of activities to continue in the

state, it cannot change the rules after an activity has begun. If those rules are changed, the incentives will not be factored in when businesses determine where to conduct an activity, such as R&D and manufacturing. As a result, Connecticut, with its high costs, is likely to lose out. We urge you to further scrutinize the proposed budget to find additional costs savings and to reject harmful tax measures that would:

- Reduce the value of investment incentives for research and development, capital purchases, and other key economic drivers;
- Reduce the net operating loss carry-forward, an important tax mechanism to encourage investment in Connecticut;
- Continue indefinitely the 20% corporate surcharge that was scheduled to be illuminated this year;
- Continue the credit reduction for the insurance tax that was scheduled to be illuminated this year; and
- Increase numerous fees paid by businesses.

Connecticut can be a top destination for business, but we need to encourage rather than discourage investment that leads to job creation.

If the abovementioned proposals are rejected, before you today are several other measures that will help increase economic activity and generate both revenues and jobs in Connecticut. These include:

- **SB 323** An Act Increasing The Annual Cap On The Neighborhood Assistance Act Tax Credit Program;
- **SB 329** An Act Concerning A Manufacturing Scholarship Tax Credit;
- **SB 540** An Act Increasing The Aggregate Cap On Insurance Reinvestment Fund Tax Credits And Renaming Such Funds Invest CT Funds;
- **SB 546** An Act Extending The Manufacturing Apprenticeship And R.E. Van Norstrand Neighborhood Assistance Act Tax Credits To Pass-Through Entities;
- **HB 5978** An Act Expanding The Research And Development Tax Credit For Bioscience Companies.

My testimony for each of these measures follows on separate pages.

SB 323 - An Act Increasing The Annual Cap On The Neighborhood Assistance Act Tax Credit Program

Have you ever walked by the Goodspeed Opera House on a beautiful spring day and seen numerous school-age children sitting at a picnic table rehearsing their lines? That was probably just one activity that was the result of a lot of hard work on the part of the theater, and a charitable donation made by a Connecticut company or individual.

While most of us are not even aware of it, the Connecticut Neighborhood Assistance Act (NAA) has helped make Connecticut a better place for us all to live and work. There are numerous recipients scattered throughout the state that bring us enjoyment and improve our quality of life.

All types of economic incentives play a vital role in encouraging the types of behavior we want to see in our state. Whether it is for research and development, historic home rehabilitation, or giving to local charitable organizations, such tax policies make Connecticut a better place to live and work.

According to CNBC, Connecticut ranks 14th out of the 50 states in our “Quality of Life.” Measures such as this NAA proposal can help improve that ranking. CBIA supports **SB 323**, An Act Increasing The Annual Cap On The Neighborhood Assistance Act Tax Credit Program as a step in the right direction because it will increase the NAA total cap from \$5 million to \$10 million, and that’s a step in the right direction.

We urge your support of **SB 323**.

Thank you.

SB 329 - An Act Concerning A Manufacturing Scholarship Tax Credit

Manufacturing is vital to Connecticut's future because manufacturers are powerful sources of economic activity and innovation. It is important, therefore, that state tax policy encourages those activities (innovation and growth) to take place in Connecticut. That's why CBIA is urging you to support **SB 329**, An Act Concerning A Manufacturing Scholarship Tax Credit, to help offset some of the costs of sending a student through the state's manufacturing program and increase interest in manufacturing among Connecticut's youth.

A recent survey of manufacturers identified at least 1,000 existing vacancies in key manufacturing positions. The survey also showed that by the end of this year, manufacturers expect to hire over 1,400 people in those key positions. These are well paying jobs with benefits, but we need to interest more people in learning about the available opportunities, and we need to create more incentives to train individuals in Connecticut.

According to CNBC, in 2014 Connecticut tied for 32nd out of 50 in the "Workforce" category of the state economic competitiveness rankings. One of the areas that Connecticut does not currently score well in is our ability to place graduates with employers. With that in mind, there are positions that desperately need to be filled. Connecticut could improve in this area if we work to align graduates with the opportunities that await them.

Expanding access to manufacturing programs through scholarships and tax credits would be a win-win situation: Manufacturers want to invest in training current and new employees, but often lack the resources to do it.

With Connecticut's aging manufacturing workforce population heading toward retirement, and with a shortage of up-and-coming skilled talent, many good jobs and careers are going unfilled.

SB 329 - An Act Concerning A Manufacturing Scholarship Tax Credit (Cont.)

Connecticut manufacturers are powerful sources of economic activity and drivers of innovation. Keeping them competitive means adopting this kind of measure that will help them grow and create more jobs.

I urge you to support **SB 329**.

Thank you.

SB 540 - An Act Increasing The Aggregate Cap On Insurance Reinvestment Fund Tax Credits And Renaming Such Funds Invest CT Funds

Five years ago, there were a great many questions surrounding the state's Insurance Reinvestment Fund (IRF) program. These questions included whether it should exist, were modifications needed, etc.? In the end, the Majority Leaders' Roundtable decided to make a number of changes to improve the IRF.

What a good idea! The IRF now uses tax incentives to help match investors and businesses. Because the credits can only be applied against the state's premium tax, the measure encourages Connecticut insurance companies to invest in other Connecticut-based job creators.

This program has worked very well for Connecticut for the past five years. We have seen investments in biopharma, aerospace, and more--all of which the types of companies that are economic drivers and can help make Connecticut's economy better.

According to CNBC, Connecticut ties for seventh place out of the 50 states when it comes to "Access to Capital." That is one of our better rankings, but we can do better. This measure will help Connecticut-based companies gain greater access to capital.

I urge you to approve **SB 540**, An Act Increasing The Aggregate Cap On Insurance Reinvestment Fund Tax Credits And Renaming Such Funds Invest CT Funds. Working together, we can make Connecticut more economically competitive. Please support **SB 540**.

Thank you.

SB 546 - An Act Extending The Manufacturing Apprenticeship And R.E. Van Norstrand Neighborhood Assistance Act Tax Credits To Pass-Through Entities

I appreciate your hearing **SB 546**. If dollars were unlimited, this would be a perfect piece of legislation. However, dollars are not unlimited, so I ask that you modify the measure before you to address the acute needs of Connecticut's small and midsize business community.

Manufacturing is vital to Connecticut's future because manufacturers are powerful sources of economic activity and innovation. Unfortunately, there is a significant manufacturing workforce shortage in the state.

In a survey conducted by CBIA, Connecticut manufacturers identified at least 1,000 existing vacancies in key manufacturing positions. The survey also showed that by the end of 2015, manufacturers expect to hire over 1,400 people in those key positions. This is a significant concern. To make matters worse, according to the state Department of Labor, there were only 85 active apprenticeship sponsors at Connecticut's pass-through entities (S Corporations, Limited Liability Corporations, and Limited Liability Partnerships) in the manufacturing sector, and 150 apprentices in total.

Last year, legislation was adopted to permit pass-through entities to earn an apprenticeship tax credit, but this hasn't worked as smoothly as is needed for the program to succeed. As drafted, pass-through entities earn the credit, but then must sell it to a C corporation for less than face value. Furthermore, the market for purchasing C corporation credits is not particularly strong.

Fixing the apprenticeship tax credit for pass-through entities as soon as possible is extremely important because of the serious workforce shortages facing Connecticut manufacturers. Therefore, we would appreciate it if you would modify existing law to permit pass-through entities to apply the credit against taxes due the state, other than the Personal Income Tax, or permit them to sell the earned credits to companies that can apply such a credit against their gross-earnings tax.

While this proposal is modest, it is an extremely important measure and is desperately needed.

Please modify this measure to reflect the changes I have requested and approve it so that we can begin taking the steps needed to ensure we have the workforce needed to meet Connecticut's manufacturing demands.

Thank you.

**HB 5978 - An Act Expanding The Research And Development Tax Credit For Bioscience
Companies**

Innovation

Research and development (R&D) is crucial to both the short term vitality and the long term health of any business. Because the economic well-being of the state is strongly tied to innovation and sustained business growth, eliminating the caps on R&D tax credits as well as extending them to pass-through entities would contribute to the state's economic recovery.

The R&D tax credit is the state's primary tax policy fostering innovation and driving sustainable job growth. But the R&D process is long and costly. Therefore, R&D tax credits are critical to locating such facilities in the state.

What Is the R&D Tax Credit and Who Can Utilize It?

The R&D tax credit is earned by making by investments in Connecticut R&D jobs or facilities as specified by the legislature. The credits were established to encourage specific investment in Connecticut and have resulted in a significant increase in R&D jobs in Connecticut. The credit can only be claimed for specific research and development investments and activities conducted in Connecticut and only after the investment targeted has been made. Since the research and development period for most products is extremely long, there is usually no cost to Connecticut until months or years after an in-state investment is made.

Credits are an important mechanism for offsetting costs where Connecticut may not be competitive. Connecticut must compete for investment, since many other states and foreign jurisdictions also offer credit programs. Credits are important considerations in decisions of where to locate investment.

Credits benefit only those in-state companies that make the investment in those in-state jobs and facilities, which generate economic growth in Connecticut. Limiting tax credits, including by cutting the carry-forward period, raises taxes only on those in-state companies that have made the investment the legislature is trying to encourage. Such actions depress economic growth in Connecticut.

R&D Carry-forward Is Important in Anchoring Businesses to Connecticut

The R&D tax credit is the state's primary tax policy fostering innovation, and innovation drives sustainable job growth. The R&D tax credit carry-forward helps anchor

HB 5978 - AA Expanding The R&D Tax Credit For Bioscience Companies (Cont.)

businesses to Connecticut because long R&D and product cycles require matching carry-forward conditions. A company only earns value for carry-forward by continuing to produce income in the state.

CT Industries	CT R&D Cycle	CT Manufacturing Cycle
Pharmaceuticals	7-15 years	7-8 years
Aerospace	5-20 years	30+ years
Submarines	5-7 years	30+ years

15 Years of Research Often Doesn't Mean the Next 15 Years Will Bring Profit

From the chart above, one can see that the R&D phase of a product is rarely, if ever, short. Companies are in the research and experiment stage for years.

The average research cycle in the pharmaceutical industry is seven to 15 years. New drugs take years from discovery of the initial molecule to a marketable medication. Even after all that time, it can be years before the company begins to earn a profit on the product.

The aerospace industry has an even longer R&D time frame. For most aerospace products, it runs from 5 to 20 years. Under the proposal before you today, the opportunity to take the R&D tax credit for years of investments has been eliminated before the product even reaches the market. What's more, as in the pharmaceutical industry, even when the product has reached the market, it can easily take many more years before the company earns a profit on the product.

A real-life example of the challenges companies face, and why the 15-year time limit on carry-forwards doesn't work, is included in the attached presentation. In it, an aerospace company explains that its R&D phase for one new product lasted for 20 years. The company has invested over \$1 billion in the product and it is just now reaching the production stage.

HB 5978 - AA Expanding The R&D Tax Credit For Bioscience Companies (Cont.)

Long-Term Vitality of R&D Credits Is Critical Keeping R&D in Connecticut

Although well intentioned, the Governor's proposal to limit R&D credits further and the limitations he proposed placing on the Net Operating Loss Carryforward period in Connecticut would be devastating. I hope the explanation of the time cycles, as well as recognizing that every attempt to create a workable product does not pan out, gives you a better understanding of why the proposal to limit the carry-forward should be rejected. Connecticut has already diminished the vitality of the R&D tax credit by imposing a 70% credit cap. I urge you to reject any efforts to limit this credit further. The R&D industry is too important to Connecticut to limit such credits, or to limit the carry-forward, as proposed by the Governor.

Please eliminate the caps on Connecticut's R&D tax credits and extend them to pass-through entities.

Thank you.

Conclusion

Consistency, clarity, and fairness in state tax policy are achievable and critically important goals. We urge you to reject the Governor's revenue proposals and adopt the measures mentioned above that can help unlock much-needed business investment and job growth by implementing certain improvements. Doing so will help create a more predictable and fairer tax environment, and a more competitive Connecticut economy.

Thank you for your consideration