

2018 -- S 2665

LC004944

STATE OF RHODE ISLAND

IN GENERAL ASSEMBLY

JANUARY SESSION, A.D. 2018

A N A C T

RELATING TO STATE AFFAIRS AND GOVERNMENT - ESTABLISHING A SMALL
BUSINESS DEVELOPMENT FUND

Introduced By: Senators Conley, Sosnowski, DiPalma, Seveney, and Lombardo

Date Introduced: March 20, 2018

Referred To: Senate Finance

It is enacted by the General Assembly as follows:

1 SECTION 1. Title 42 of the General Laws entitled "STATE AFFAIRS AND
2 GOVERNMENT" is hereby amended by adding thereto the following chapter:

3 CHAPTER 64.33

4 THE RHODE ISLAND SMALL BUSINESS DEVELOPMENT FUND

5 **42-64.33-1. Short title.**

6 This chapter shall be known and may be cited as the "Rhode Island Small Business
7 Development Fund."

8 **42-64.33-2. Findings and purpose.**

9 (a) It is hereby found that across the nation, small businesses account for up to sixty-six
10 percent (66%) of all new jobs created annually. The Rhode Island economy is no different.
11 Consequently, a need exists for a small business development program that complements existing
12 traditional lending and investment sources to fill the widening gap of financing largely
13 unavailable to the state's many small businesses and startups. Through the establishment of the
14 small business development fund, Rhode Island will attract private investment dollars for "Main
15 Street" small businesses and stimulate growth across a breadth of industries including future-
16 oriented industries strategically identified as promising potential sources of sustainable economic
17 growth for Rhode Island.

18 (b) Small and startup businesses in this state have found it difficult to attract capital

1 necessary to make investments that would stimulate economic development activity and create
2 new jobs for the citizens of the state. Consequently, a need exists to attract capital that promotes
3 the retention and expansion of existing jobs, stimulates the creation of new jobs, attracts new
4 business and industry to the state, and stimulates growth in businesses that are prepared to make
5 meaningful investments and foster job creation.

6 (c) Through the establishment of a small business development fund tax credit program,
7 Rhode Island can take steps to attract capital to stimulate venture, growth, and expansion-stage
8 investment, retain and attract new business and industry to the state, create good-paying jobs, and
9 stimulate growth in startup businesses and other businesses that are poised for growth.

10 **42-64.33-3. Definitions.**

11 (a) As used in this chapter:

12 (1) “Affiliate” means an entity that directly, or indirectly, through one or more
13 intermediaries, controls, or is controlled by, or is under common control with another entity. For
14 the purposes of this chapter, an entity is “controlled by” another entity if the controlling entity
15 holds, directly or indirectly, the majority voting or ownership interest in the controlled entity or
16 has control over the day-to-day operations of the controlled entity by contract or by law.

17 (2) “Applicable percentage” means zero percent (0%) for the first three (3) credit
18 allowance dates, and twenty-one and one-half percent (21.5%) for the fourth, fifth, and sixth
19 credit allowance dates.

20 (3) “Capital investment” means any equity investment in a small business development
21 fund by a small business fund investor that:

22 (i) Is acquired after the effective date of this chapter at its original issuance solely in
23 exchange for cash;

24 (ii) Has one hundred percent (100%) of its cash purchase price used by the small business
25 development fund to make qualified investments in eligible businesses located in this state within
26 three (3) years of the initial credit allowance date; and

27 (iii) Is designated by the small business development fund as a capital investment under
28 this chapter and is certified by the department pursuant to § 42-64.33-5. This term shall include
29 any capital investment that does not meet the provisions of § 42-64.33-5(a) if the investment was
30 a capital investment in the hands of a prior holder.

31 (4) “Credit allowance date” means the date on which a capital investment is made and
32 each of the five (5) anniversary dates of the date thereafter.

33 (5) “Department” means the Rhode Island commerce corporation.

34 (6) “Eligible business” means a business that, at the time of the initial qualified

1 investment in the company:

2 (i) Has less than two hundred fifty (250) employees;

3 (ii) Has not more than fifteen million dollars (\$15,000,000) in net income from the
4 preceding tax year;

5 (iii) Has its principal business operations in this state; and

6 (iv) Is engaged in industries related to clean energy, biomedical innovation, life sciences,
7 information technology, software, cyber physical systems, cybersecurity, data analytics, defense,
8 shipbuilding, maritime, composites, advanced business services, design, food, manufacturing,
9 transportation, distribution, logistics, arts, education, hospitality, tourism, or, if not engaged in the
10 industries, the department makes a determination that the investment will be beneficial to the
11 economic growth of the state.

12 (7) "Eligible distribution" means:

13 (i) A distribution of cash to one or more equity owners of a small business fund investor
14 to fully or partially offset a projected increase in the owner's federal or state tax liability,
15 including any penalties and interest, related to the owner's ownership, management, or operation
16 of the small business fund investor;

17 (ii) A distribution of cash as payment of interest and principal on the debt of the small
18 business fund investor or small business development fund; or

19 (iii) A distribution of cash related to the reasonable costs and expenses of forming,
20 syndicating, managing, and operating the small business fund investor or the small business
21 development fund, or a return of equity to affiliates of a small business fund investor or small
22 business development fund. The distributions may include reasonable and necessary fees paid for
23 professional services, including legal and accounting services, related to the formation and
24 operation of the small business development fund.

25 (8) "Jobs created" means a newly created position of employment that was not previously
26 located in the state at the time of the qualified investment in the eligible business and requiring a
27 minimum of thirty five (35) hours worked each week, measured each year by subtracting the
28 number of employment positions at the time of the initial qualified investment in the eligible
29 business from the monthly average of employment positions for the applicable year. The number
30 shall not be less than zero.

31 (9) "Jobs retained" means a position requiring a minimum of thirty five (35) hours
32 worked each week that existed prior to the initial qualified investment. Retained jobs shall be
33 counted each year based on the monthly average of employment positions for the applicable year.
34 The number shall not exceed the initial amount of retained jobs reported and shall be reduced

1 each year if employment at the eligible business concern drops below that number.

2 (10) "Principal business operations" means the location where at least sixty percent
3 (60%) of a business's employees work or where employees who are paid at least sixty percent
4 (60%) percent of the business's payroll work. A business that has agreed to relocate employees
5 using the proceeds of a qualified investment to establish its principal business operations in a new
6 location shall be deemed to have its principal business operations in the new location if it satisfies
7 these requirements no later than one hundred eighty (180) days after receiving a qualified
8 investment.

9 (11) "Purchase price" means the amount paid to the small business development fund that
10 issues a capital investment which shall not exceed the amount of capital investment authority
11 certified pursuant to § 42-64.33-5.

12 (12) "Qualified investment" means any investment in an eligible business or any loan to
13 an eligible business with a stated maturity date of at least one year after the date of issuance,
14 excluding revolving lines of credit and senior secured debt unless the eligible business has a
15 credit refusal letter or similar correspondence from a depository institution or a referral letter or
16 similar correspondence from a depository institution referring the business to a small business
17 development fund; provided that, with respect to any one eligible business, the maximum amount
18 of investments made in the business by one or more small business development funds, on a
19 collective basis with all of the businesses' affiliates, with the proceeds of capital investments shall
20 be twenty percent (20%) of the small business development fund's capital investment authority,
21 exclusive of investments made with repaid or redeemed investments or interest or profits realized
22 thereon. An eligible business, on a collective basis with all of the businesses' affiliates, is
23 prohibited from receiving more than four million dollars (\$4,000,000) in investments from one or
24 more small business development funds with the proceeds of capital investments.

25 (13) "Small business development fund" means an entity certified by the department
26 under § 42-64.33-5.

27 (14) "Small business fund investor" means an entity that makes a capital investment in a
28 small business development fund.

29 (15) "State" means the state of Rhode Island and Providence Plantations.

30 (16) "State tax liability" means any liability incurred by any entity under § 44-17-1 et
31 seq., § 27-2-17 or, if the taxes are eliminated or reduced, the term shall also mean any tax liability
32 imposed on an entity or other person that had tax liability under the laws of this state.

33 **42-64.33-4. Tax credit established.**

34 (a) Upon making a capital investment in a small business development fund, a small

1 business fund investor earns a vested right to a credit against the entity's state tax liability that
2 may be utilized on each credit allowance date of the capital investment in an amount equal to the
3 applicable percentage for the credit allowance date multiplied by the purchase price paid to the
4 small business development fund for the capital investment. The amount of the credit claimed by
5 a small business fund investor shall not exceed the amount of the entity's state tax liability for the
6 tax year for which the credit is claimed. Any amount of credit that a small business investor is
7 prohibited from claiming in a taxable year as a result of this section may be carried forward for
8 use in any subsequent taxable year. It is the intent of this chapter that a small business investor
9 claiming a credit under this section is not required to pay any additional tax that may arise as a
10 result of claiming the credit.

11 (b) No credit claimed under this section shall be refundable or saleable on the open
12 market. Credits earned by or allocated to a partnership, limited liability company, or S
13 corporation may be allocated to the partners, members, or shareholders of the entity for their
14 direct use in accordance with the provisions of any agreement among the partners, members, or
15 shareholders, and a small business development fund must notify the department of the names of
16 the entities that are eligible to utilize credits pursuant to an allocation of credits or a change in
17 allocation of credits or due to a transfer of a capital investment upon the allocation, change, or
18 transfer. The allocation shall be not considered a sale for purposes of this section. Interest in a
19 partnership, limited liability company, or S corporation may be earned by the purchase of an
20 equity interest in the partnership, limited liability company or S corporation or the purchase of a
21 debt instrument issued by the partnership, limited liability company, or S corporation.

22 **42-64.33-5. Application, approval and allocations.**

23 (a) A small business development fund that seeks to have an equity investment certified
24 as a capital investment and eligible for credits under this chapter shall apply to the department.
25 The department shall begin accepting applications within ninety (90) days of the effective date of
26 this chapter. The small business development fund shall include the following:

27 (1) The amount of capital investment requested;

28 (2) A copy of the applicant's or an affiliate of the applicant's license as a rural business
29 investment company under 7 U.S.C. § 2009cc, or as a small business investment company under
30 15 U.S.C. § 681, and a certificate executed by an executive officer of the applicant attesting that
31 the license remains in effect and has not been revoked;

32 (3) Evidence that, as of the date the application is submitted, the applicant or affiliates of
33 the applicant have invested at least one hundred million dollars (\$100,000,000) in nonpublic
34 companies;

1 (4) An estimate of the number of jobs that will be created or retained in this state as a
2 result of the applicant's qualified investments;

3 (5) A business plan that includes a revenue impact assessment projecting state and local
4 tax revenue to be generated by the applicant's proposed qualified investment prepared by a
5 nationally recognized, third-party, independent economic forecasting firm using a dynamic
6 economic forecasting model that analyzes the applicant's business plan over the ten (10) years
7 following the date the application is submitted to the department; and

8 (6) A nonrefundable application fee of five thousand dollars (\$5,000), payable to the
9 department.

10 (b) Within thirty (30) days after receipt of a completed application, the department shall
11 grant or deny the application in full or in part. The department shall deny the application if:

12 (1) The applicant does not satisfy all of the criteria described in subsection (a) of this
13 section;

14 (2) The revenue impact assessment submitted with the application does not demonstrate
15 that the applicant's business plan will result in a positive economic impact on this state over a ten
16 (10) year period that exceeds the cumulative amount of tax credits that would be issued to the
17 applicant if the application were approved; or

18 (3) The department has already approved the maximum amount of capital investment
19 authority under subsection (f) of this section.

20 (c) If the department denies any part of the application, it shall inform the applicant of the
21 grounds for the denial. If the applicant provides any additional information required by the
22 department or otherwise completes its application within fifteen (15) days of the notice of denial,
23 the application shall be considered completed as of the original date of submission. If the
24 applicant fails to provide the information or fails to complete its application within the fifteen
25 (15) day period, the application remains denied and must be resubmitted in full with a new
26 submission date.

27 (d) If the application is complete, the department shall certify the proposed equity
28 investment as a capital investment that is eligible for credits under this chapter, subject to the
29 limitations contained in subsection (g) of this section. The department shall provide written notice
30 of the certification to the small business development fund.

31 (e) The department shall certify capital investments in the order that the applications were
32 received by the department. Applications received on the same day shall be deemed to have been
33 received simultaneously.

34 (f) For applications that are complete and received on the same day, the department shall

1 certify applications in proportionate percentages based upon the ratio of the amount of capital
2 investments requested in an application to the total amount of capital investments requested in all
3 applications.

4 (g) The department shall certify sixty-five million dollars (\$65,000,000) in capital
5 investments pursuant to this section; provided that not more than twenty million dollars
6 (\$20,000,000) may be allocated to any individual small business development fund certified
7 under this section.

8 (h) Within sixty (60) days of the applicant receiving notice of certification, the small
9 business development fund shall issue the capital investment to and receive cash in the amount of
10 the certified amount from a small business fund investor. At least forty-five percent (45%) of the
11 small business fund investor's capital investment shall be composed of capital raised by the small
12 business fund investor from sources, including directors, members, employees, officers, and
13 affiliates of the small business fund investor, other than the amount of capital invested by the
14 allocatee claiming the tax credits in exchange for the allocation of tax credits; provided that at
15 least ten percent (10%) of the capital investment shall be derived from the small business
16 investment fund's managers. The small business development fund shall provide the department
17 with evidence of the receipt of the cash investment within sixty-five (65) days of the applicant
18 receiving notice of certification. If the small business development fund does not receive the cash
19 investment and issue the capital investment within the time period following receipt of the
20 certification notice, the certification shall lapse and the small business development fund shall not
21 issue the capital investment without reapplying to the department for certification. Lapsed
22 certifications revert to the authority and shall be reissued pro rata to applicants whose capital
23 investment allocations were reduced pursuant to § 42-64.33-5(f) and then in accordance with the
24 application process.

25 **42-64.33-6. Tax credit recapture and exit.**

26 (a) The department may recapture, from a small business fund investor that claimed the
27 credit on a tax return, the credit allowed under § 42-64.33-5 if:

28 (1) The small business development fund does not invest one hundred (100%) percent of
29 its capital investment authority in qualified investments in this state within three (3) years of the
30 first credit allowance date;

31 (2) The small business development fund, after satisfying subsection (a)(1) of this
32 section, fails to maintain qualified investments equal to one hundred (100%) percent of its capital
33 investment authority until the sixth anniversary of the initial credit allowance date. For the
34 purposes of this subsection, a qualified investment is considered maintained even if the qualified

1 investment was sold or repaid so long as the small business development fund reinvests an
2 amount equal to the capital returned or recovered by the small business development fund from
3 the original investment, exclusive of any profits realized, in other qualified investments in this
4 state within twelve (12) months of the receipt of the capital. Amounts received periodically by a
5 small business development fund shall be treated as continually invested in qualified investments
6 if the amounts are reinvested in one or more qualified investments by the end of the following
7 calendar year. A small business development fund shall not be required to reinvest capital
8 returned from qualified investments after the fifth anniversary of the initial credit allowance date,
9 and the qualified investments shall be considered held continuously by the small business
10 development fund through the sixth anniversary of the initial credit allowance date;

11 (3) The small business development fund, before exiting the program in accordance with
12 § 42-64.33-6(e), makes a distribution or payment that results in the small business development
13 fund having less than one hundred percent (100%) of its capital investment authority invested in
14 qualified investments in this state or available for investment in qualified investments and held in
15 cash and other marketable securities; or

16 (4) The small business development fund violates subsection (d) of this section.

17 (b) Recaptured credits and the related capital investment authority revert to the
18 department and shall be reissued pro rata to applicants whose capital investment allocations were
19 reduced pursuant to subsection (g) of this section and then in accordance with the application
20 process.

21 (c) Enforcement of each of the recapture provisions of subsection (a) of this section shall
22 be subject to a six (6) month cure period. No recapture shall occur until the small business
23 development fund has been given notice of noncompliance and afforded six (6) months from the
24 date of the notice to cure the noncompliance.

25 (d) No eligible business that receives a qualified investment under this chapter, or any
26 affiliates of the eligible business, may directly or indirectly:

27 (1) Own or have the right to acquire an ownership interest in a small business
28 development fund or member or affiliate of a small business development fund, including, but not
29 limited to, a holder of a capital investment issued by the small business development fund; or

30 (2) Loan to or invest in a small business development fund or member or affiliate of a
31 small business development fund, including, but not limited to, a holder of a capital investment
32 issued by a small business development fund, where the proceeds of the loan or investment are
33 directly or indirectly used to fund or refinance the purchase of a capital investment under this
34 chapter.

1 (e) On or after the sixth anniversary of the initial credit allowance date, a small business
2 development fund may apply to the department to exit the program and no longer be subject to
3 regulation under this chapter. The department shall respond to the exit application within thirty
4 (30) days of receipt. In evaluating the exit application, the fact that no credits have been
5 recaptured and that the small business development fund has not received a notice of recapture
6 that has not been cured pursuant to subsection (c) of this section shall be sufficient evidence to
7 prove that the small business development fund is eligible for exit. The department shall not
8 unreasonably deny an exit application submitted under this subsection. If the exit application is
9 denied, the notice shall include the reasons for the determination.

10 (f) If the number of jobs created or retained by the eligible businesses that received
11 qualified investments from the small business development fund, calculated pursuant to reports
12 filed by the small business development fund pursuant to § 42-64.33-8, is:

13 (1) Less than sixty percent (60%) of the amount projected in the approved small business
14 development fund's business plan filed as part of its application for certification under § 42-
15 64.33-5, then the state shall receive thirty percent (30%) of any distribution or payment to an
16 equity holder in an approved small business development fund in excess of eligible distributions;
17 or

18 (2) Greater than sixty percent (60%) but less than one hundred percent (100%) of the
19 amount projected in the approved small business development fund's business plan filed as part
20 of its application for certification under § 42-64.33-5, then the state shall receive fifteen percent
21 (15%) of any distribution or payment to an equity holder in an approved small business
22 development fund in excess of eligible distributions.

23 (g) At the time a small business development fund applies to the department to exit the
24 program, it shall calculate the aggregate internal rate of return of its qualified investments. If the
25 small business development fund's aggregate internal rate of return on its qualified investments at
26 exit exceeds ten percent (10%), then, after eligible distributions, the state shall receive ten percent
27 (10%) of any distribution or payment in excess of the aggregate ten percent (10%) internal rate of
28 return to an equity holder in an approved small business development fund.

29 (h) The department shall not revoke a tax credit certificate after the small business
30 development fund's exit from the program.

31 **42-64.33-7. Request for determination.**

32 (a) A small business development fund, before making a qualified investment, may
33 request from the department a written opinion as to whether the business in which it is proposed
34 to invest is an eligible business. The department, not later than the fifteenth business day after the

1 date of receipt of the request, shall notify the small business development fund of its
2 determination. If the department fails to notify the small business development fund by the
3 fifteenth business day of its determination, the business in which the small business development
4 fund proposes to invest shall be considered an eligible business.

5 **42-64.33-8. Reporting obligations.**

6 (a) Each small business development fund shall submit a report to the department and the
7 division of taxation on or before the fifth business day after the second anniversary of the closing
8 date. The report shall provide documentation as to the small business development fund's
9 qualified investments and include:

10 (1) A bank statement evidencing each qualified investment;

11 (2) The name, location, and industry of each business receiving a qualified investment,
12 including either the determination letter set forth in § 42-64.33-7 or evidence that the business
13 qualified as an eligible business at the time the investment was made; and

14 (3) The number of employment positions created or retained as a result of the small
15 business development fund's qualified investments as of the last day of the preceding calendar
16 year;

17 (b) On or before the last day of February of each year following the year in which the
18 report required in subsection (a) of this section is due, the small business development fund shall
19 submit an annual report to the department and the division of taxation including the following:

20 (1) The number of employment positions created or retained as a result of the small
21 business development fund's qualified investments as of the last day of the preceding calendar
22 year;

23 (2) The average annual salary of the positions described in subsection (b)(1) of this
24 section; and

25 (3) The follow-on capital investment that has occurred along with or after the small
26 business development fund's investment as of the last day of the preceding calendar year.

27 (c) A copy of the reports required under this section must also be sent concurrently to the
28 speaker of the house, president of the senate, house finance chairperson, senate finance
29 chairperson, and the general treasurer.

30 **42-64.33-9. Rules and regulations.**

31 The department and division of taxation may issue reasonable rules and regulations,
32 consistent with this chapter, as are necessary to carry out the intent and purpose and
33 implementation of the responsibilities under this chapter.

1 SECTION 2. This act shall take effect upon passage.

=====
LC004944
=====

EXPLANATION
BY THE LEGISLATIVE COUNCIL
OF
A N A C T
RELATING TO STATE AFFAIRS AND GOVERNMENT - ESTABLISHING A SMALL
BUSINESS DEVELOPMENT FUND

1 This act would establish a small business development fund designed to encourage the
2 formation of private capital investment by federally licensed investment companies in
3 underserved small businesses, leveraged by delayed, at-risk stream of tax credits applicable
4 against insurance premium and retaliatory taxes that can be recaptured for noncompliance with
5 program investment requirements. Monetary penalties would exist if job creation and retention
6 projections would be missed, and the state shares in profits above a certain level of fund returns.
7 Investments would be designated for targeted growth industries for the state, and would be
8 required to be diversified – no one small business would receive more than four (\$4,000,000)
9 million or twenty percent (20%) of a fund’s investment authority. The investment funds would
10 report annually, and the program would terminate after six (6) years.

11 This act would take effect upon passage.

=====
LC004944
=====