

2018 -- S 2665 SUBSTITUTE A

LC004944/SUB A

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. Definitions.**

9 (a) As used in this chapter:

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

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

18 (3) "Capital investment" means any equity investment in a small business development

1 fund by a small business fund investor that:

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

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

7 (iii) Is designated by the small business development fund as a capital investment under
8 this chapter and is certified by the department pursuant to § 42-64.33-4. This term shall include
9 any capital investment that does not meet the provisions of § 42-64.33-4(a) if the investment was
10 a capital investment in the hands of a prior holder.

11 (4) "Credit allowance date" means the date on which a capital investment is made and
12 each of the five (5) anniversary dates of the date thereafter.

13 (5) "Department" means the Rhode Island commerce corporation.

14 (6) "Eligible business" means a business that, at the time of the initial qualified
15 investment in the company:

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

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

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

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

26 (7) "Eligible distribution" means:

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

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

33 (iii) A distribution of cash related to the reasonable costs and expenses of forming,
34 syndicating, managing, and operating the small business fund investor or the small business

1 development fund, or a return of equity to affiliates of a small business fund investor or small
2 business development fund. The distributions may include reasonable and necessary fees paid for
3 professional services, including legal and accounting services, related to the formation and
4 operation of the small business development fund.

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

11 (9) "Jobs retained" means a position requiring a minimum of thirty five (35) hours
12 worked each week that existed prior to the initial qualified investment. Retained jobs shall be
13 counted each year based on the monthly average of employment positions for the applicable year.
14 The number shall not exceed the initial amount of retained jobs reported and shall be reduced
15 each year if employment at the eligible business concern drops below that number.

16 (10) "Minority business enterprise" means a small business concern which is certified by
17 the Rhode Island office of diversity, equity and opportunity as being a minority or women
18 business enterprise.

19 (11) "Principal business operations" means the location where at least sixty percent
20 (60%) of a business's employees work or where employees who are paid at least sixty percent
21 (60%) percent of the business's payroll work. A business that has agreed to relocate employees
22 using the proceeds of a qualified investment to establish its principal business operations in a new
23 location shall be deemed to have its principal business operations in the new location if it satisfies
24 these requirements no later than one hundred eighty (180) days after receiving a qualified
25 investment.

26 (12) "Purchase price" means the amount paid to the small business development fund that
27 issues a capital investment which shall not exceed the amount of capital investment authority
28 certified pursuant to § 42-64.33-4.

29 (13) "Qualified investment" means any investment in an eligible business or any loan to
30 an eligible business with a stated maturity date of at least one year after the date of issuance,
31 excluding revolving lines of credit and senior secured debt unless the eligible business has a
32 credit refusal letter or similar correspondence from a depository institution or a referral letter or
33 similar correspondence from a depository institution referring the business to a small business
34 development fund; provided that, with respect to any one eligible business, the maximum amount

1 of investments made in the business by one or more small business development funds, on a
2 collective basis with all of the businesses' affiliates, with the proceeds of capital investments shall
3 be twenty percent (20%) of the small business development fund's capital investment authority,
4 exclusive of investments made with repaid or redeemed investments or interest or profits realized
5 thereon. An eligible business, on a collective basis with all of the businesses' affiliates, is
6 prohibited from receiving more than four million dollars (\$4,000,000) in investments from one or
7 more small business development funds with the proceeds of capital investments.

8 (14) "Small business development fund" means an entity certified by the department
9 under § 42-64.33-4.

10 (15) "Small business fund investor" means an entity that makes a capital investment in a
11 small business development fund.

12 (16) "State" means the state of Rhode Island and Providence Plantations.

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

16 **42-64.33-3. Tax credit established.**

17 (a) Upon making a capital investment in a small business development fund, a small
18 business fund investor earns a vested right to a credit against the entity's state tax liability that
19 may be utilized on each credit allowance date of the capital investment in an amount equal to the
20 applicable percentage for the credit allowance date multiplied by the purchase price paid to the
21 small business development fund for the capital investment. The amount of the credit claimed by
22 a small business fund investor shall not exceed the amount of the entity's state tax liability for the
23 tax year for which the credit is claimed. Any amount of credit that a small business investor is
24 prohibited from claiming in a taxable year as a result of this section may be carried forward for
25 use in any subsequent taxable year. It is the intent of this chapter that a small business investor
26 claiming a credit under this section is not required to pay any additional tax that may arise as a
27 result of claiming the credit.

28 (b) No credit claimed under this section shall be refundable or saleable on the open
29 market. Credits earned by or allocated to a partnership, limited liability company, or S
30 corporation may be allocated to the partners, members, or shareholders of the entity for their
31 direct use in accordance with the provisions of any agreement among the partners, members, or
32 shareholders, and a small business development fund must notify the department of the names of
33 the entities that are eligible to utilize credits pursuant to an allocation of credits or a change in
34 allocation of credits or due to a transfer of a capital investment upon the allocation, change, or

1 transfer. The allocation shall be not considered a sale for purposes of this section. Interest in a
2 partnership, limited liability company, or S corporation may be earned by the purchase of an
3 equity interest in the partnership, limited liability company or S corporation or the purchase of a
4 debt instrument issued by the partnership, limited liability company, or S corporation.

5 **42-64.33-4. Application, approval and allocations.**

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

10 (1) The amount of capital investment requested;

11 (2) A copy of the applicant's or an affiliate of the applicant's license as a rural business
12 investment company under 7 U.S.C. § 2009cc, or as a small business investment company under
13 15 U.S.C. § 681, and a certificate executed by an executive officer of the applicant attesting that
14 the license remains in effect and has not been revoked;

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

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

20 (5) A business plan that includes a strategy for reaching out to and investing in minority
21 business enterprises and a revenue impact assessment projecting state and local tax revenue to be
22 generated by the applicant's proposed qualified investment prepared by a nationally recognized,
23 third-party, independent economic forecasting firm using a dynamic economic forecasting model
24 that analyzes the applicant's business plan over the ten (10) years following the date the
25 application is submitted to the department; and

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

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

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

32 (2) The revenue impact assessment submitted with the application does not demonstrate
33 that the applicant's business plan will result in a positive economic impact on this state over a ten
34 (10) year period that exceeds the cumulative amount of tax credits that would be issued to the

1 applicant if the application were approved; or

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

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

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

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

18 (f) For applications that are complete and received on the same day, the department shall
19 certify applications in proportionate percentages based upon the ratio of the amount of capital
20 investments requested in an application to the total amount of capital investments requested in all
21 applications.

22 (g) The department shall certify sixty-five million dollars (\$65,000,000) in capital
23 investments pursuant to this section; provided that not more than twenty million dollars
24 (\$20,000,000) may be allocated to any individual small business development fund certified
25 under this section.

26 (h) Within sixty (60) days of the applicant receiving notice of certification, the small
27 business development fund shall issue the capital investment to and receive cash in the amount of
28 the certified amount from a small business fund investor. At least forty-five percent (45%) of the
29 small business fund investor's capital investment shall be composed of capital raised by the small
30 business fund investor from sources, including directors, members, employees, officers, and
31 affiliates of the small business fund investor, other than the amount of capital invested by the
32 allocatee claiming the tax credits in exchange for the allocation of tax credits; provided that at
33 least ten percent (10%) of the capital investment shall be derived from the small business
34 investment fund's managers. The small business development fund shall provide the department

1 with evidence of the receipt of the cash investment within sixty-five (65) days of the applicant
2 receiving notice of certification. If the small business development fund does not receive the cash
3 investment and issue the capital investment within the time period following receipt of the
4 certification notice, the certification shall lapse and the small business development fund shall not
5 issue the capital investment without reapplying to the department for certification. Lapsed
6 certifications revert to the authority and shall be reissued pro rata to applicants whose capital
7 investment allocations were reduced pursuant to this chapter and then in accordance with the
8 application process.

9 **42-64.33-5. Tax credit recapture and exit.**

10 (a) The department may recapture, from a small business fund investor that claimed the
11 credit on a tax return, the credit allowed under this chapter if:

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

15 (2) The small business development fund, after satisfying subsection (a)(1) of this
16 section, fails to maintain qualified investments equal to one hundred (100%) percent of its capital
17 investment authority until the sixth anniversary of the initial credit allowance date. For the
18 purposes of this subsection, a qualified investment is considered maintained even if the qualified
19 investment was sold or repaid so long as the small business development fund reinvests an
20 amount equal to the capital returned or recovered by the small business development fund from
21 the original investment, exclusive of any profits realized, in other qualified investments in this
22 state within twelve (12) months of the receipt of the capital. Amounts received periodically by a
23 small business development fund shall be treated as continually invested in qualified investments
24 if the amounts are reinvested in one or more qualified investments by the end of the following
25 calendar year. A small business development fund shall not be required to reinvest capital
26 returned from qualified investments after the fifth anniversary of the initial credit allowance date,
27 and the qualified investments shall be considered held continuously by the small business
28 development fund through the sixth anniversary of the initial credit allowance date;

29 (3) The small business development fund, before exiting the program in accordance with
30 subsection (e) of this section, makes a distribution or payment that results in the small business
31 development fund having less than one hundred percent (100%) of its capital investment
32 authority invested in qualified investments in this state or available for investment in qualified
33 investments and held in cash and other marketable securities;

34 (4) The small business development fund, before exiting the program in accordance with

1 subsection (e) of this section, fails to make qualified investments in minority business enterprises
2 that when added together equal at least ten percent (10%) of the small business development
3 fund's capital investment authority; or

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

5 (b) Recaptured credits and the related capital investment authority revert to the
6 department and shall be reissued pro rata to applicants whose capital investment allocations were
7 reduced pursuant to § 42-64.33-4(f) of this section and then in accordance with the application
8 process.

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

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

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

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

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

32 (f) If the number of jobs created or retained by the eligible businesses that received
33 qualified investments from the small business development fund, calculated pursuant to reports
34 filed by the small business development fund pursuant to § 42-64.33-7, is:

1 (1) Less than sixty percent (60%) of the amount projected in the approved small business
2 development fund's business plan filed as part of its application for certification under § 42-
3 64.33-4, then the state shall receive thirty percent (30%) of any distribution or payment to an
4 equity holder in an approved small business development fund in excess of eligible distributions;
5 or

6 (2) Greater than sixty percent (60%) but less than one hundred percent (100%) of the
7 amount projected in the approved small business development fund's business plan filed as part of
8 its application for certification under § 42-64.33-4, then the state shall receive fifteen percent
9 (15%) of any distribution or payment to an equity holder in an approved small business
10 development fund in excess of eligible distributions.

11 (g) At the time a small business development fund applies to the department to exit the
12 program, it shall calculate the aggregate internal rate of return of its qualified investments. If the
13 small business development fund's aggregate internal rate of return on its qualified investments at
14 exit exceeds ten percent (10%), then, after eligible distributions, the state shall receive ten percent
15 (10%) of any distribution or payment in excess of the aggregate ten percent (10%) internal rate of
16 return to an equity holder in an approved small business development fund.

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

19 **42-64.33-6. Request for determination.**

20 (a) A small business development fund, before making a qualified investment, may
21 request from the department a written opinion as to whether the business in which it is proposed
22 to invest is an eligible business. The department, not later than the fifteenth business day after the
23 date of receipt of the request, shall notify the small business development fund of its
24 determination. If the department fails to notify the small business development fund by the
25 fifteenth business day of its determination, the business in which the small business development
26 fund proposes to invest shall be considered an eligible business.

27 **42-64.33-7. Reporting obligations.**

28 (a) Each small business development fund shall submit a report to the department and the
29 division of taxation on or before the fifth business day after the third anniversary of the closing
30 date. The report shall provide documentation as to the small business development fund's
31 qualified investments and include:

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

33 (2) The name, location, status as a minority business enterprise if applicable, and industry
34 of each business receiving a qualified investment, including either the determination letter set

1 forth in § 42-64.33-6 or evidence that the business qualified as an eligible business at the time the
2 investment was made; and

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

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

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

12 (2) The number of minority business enterprises that have received qualified investments
13 and the amount of qualified investment that such minority business enterprises have received;

14 (3) The average annual salary of the positions described in subsection (b)(1) of this
15 section; and

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

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

21 **42-64.33-8. Rules and regulations.**

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

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

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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.

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