MINUTES
Tax Expenditure Committee

Tuesday, January 8, 2019

MEMBERS PRESENT

Senator Randy Feenstra, Co-chairperson
Senator Michael Breitbach (by phone)
Senator Pam Jochum
Senator Herman C. Quirmbach
Senator Roby Smith

Representative Lee Hein, Co-chairperson
Representative Jane Bloomingdale
Representative Dave Jacoby
Representative Jerry A. Kearns
Representative Matt W. Windschitl

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I. Procedural Business

Call to Order. The Tax Expenditure Committee was called to order at 10:04 a.m. on January 8, 2019, in Room 103, Supreme Court Chamber, of the State Capitol.

Adjournment. Upon conclusion of the presentations, a public comment period, and discussion by the committee, the meeting was adjourned at 1:58 p.m.

II. Charge and Introductory Comments from Co-chairpersons

Charge. The Tax Expenditure Committee was established in 2010. The committee is required to conduct regular reviews of all tax credit, withholding credit, and revenue division programs. For 2018, Iowa Code section 2.48 requires the committee to review the Child and Dependent Care and Early Childhood Development Tax Credits, property tax revenue divisions for urban renewal areas, the Redevelopment Tax Credit, and the Endow Iowa Tax Credit. The committee also agreed to review other tax credits not subject to periodic reviews under Iowa Code section 2.48.

Introductory Comments. The co-chairpersons each made brief introductory comments.

III. Review of Child Dependent Care and Early Childhood Development Tax Credits

Mr. John Good, Iowa Department of Revenue (IDR), provided background information and statistical analysis of the Iowa Child and Dependent Care (CDC) Tax Credit and the Iowa Early Childhood Development (ECD) Tax Credit.

Mr. Good described the CDC Tax Credit and the ECD Tax Credit, and provided a brief comparison of the two tax credits. The Iowa CDC Tax Credit equals between 30 and 75 percent of the federal CDC Tax Credit for families with an Iowa net income of less than $45,000. The ECD Tax Credit equals 25 percent of the first $1,000 of eligible early childhood development expenses per child between ages three and five from families with an Iowa net income of less than $45,000. Taxpayers may claim only one of the two Iowa credits in a tax year.

Mr. Good then provided the committee with general data about child care in Iowa. In 2017, the average annual cost of child care for a four-year-old child was $8,219, compared to the average annual cost of college tuition and fees of $8,759. Iowa ranks fifth highest in the United States for the percentage of children under the age of six with both parents in the labor force. In fiscal year 2017, the State of Iowa spent $76 million on the Statewide Voluntary Preschool Program. In academic year 2016-2017, the state spent $7.7 million on the Shared Visions Preschool Program.

To claim the federal and Iowa CDC Tax Credit, a taxpayer must be working or seeking employment. The federal and Iowa CDC Tax Credits are not adjusted for inflation. Unlike the federal CDC Tax Credit, the Iowa CDC Tax Credit is refundable.

Mr. Good provided a brief history of the Iowa CDC Tax Credit. The Iowa CDC Tax Credit was enacted in 1977 at 5 percent of the federal CDC Tax Credit. Iowa's credit percentage was increased to 10 percent of the federal credit in 1983, and increased to 45 percent of the federal credit in 1986. In 1990, Iowa's credit percentage was set at a sliding percentage of the federal credit. In 1993, the Iowa credit was limited to net incomes of less than $40,000. That limit was later increased to $45,000 in 2006. In 2012, the IDR's administrative rules were amended to specify that the Iowa CDC Tax Credit is to be calculated using the amount of the federal CDC Tax Credit actually received by the taxpayer, rather than the total amount the taxpayer was eligible to receive. As a result, taxpayers with no federal tax liability could no longer receive the Iowa CDC Tax Credit. In 2015, the Iowa Code was amended, allowing a taxpayer to claim Iowa's CDC Tax Credit without such federal tax liability. Mr. Good reviewed charts showing the effect these changes had on the number of claimants for each tax credit.

Mr. Good provided statistical information on recipients of the Iowa CDC Tax Credit, including income distribution, marital status, age, county of residence, and length of time the credit is received. Statewide, the utilization rates for the CDC Tax Credit and ECD Tax Credit are 15.7 percent and 11.5 percent, respectively. A CDC or ECD Tax Credit is claimed by 51.1 percent of claimants one time, while 10.5 percent of claimants take either the CDC or ECD for five or more consecutive years.

Mr. Good explained the potential impact of the tax reform enacted last year (Senate File 2417). Due to the changes in the definition of "net income," the number of households eligible to claim either the CDC or ECD Tax Credit will increase beginning in tax year 2023 (trigger year), or in a later tax year, contingent upon the satisfaction of certain net General Fund revenue amount and growth targets. If the trigger year occurs, Mr. Good stated Iowa net income for Iowa tax purposes will be computed based upon federal taxable income rather than federal adjusted gross income. This change will increase the number of claimants eligible for the CDC or ECD Tax Credit due to the new higher federal standard deduction lowering the federal taxable income for many Iowans, which in turn will place more Iowans below the net income threshold limit of $45,000 for claiming either the CDC or the ECD Tax Credit.

Discussion. Committee members expressed concerns that the CDC and ECD Tax Credits do not reduce the cost of child care enough for low-income Iowans and that wages in the state are not increasing. The committee further discussed the impact that the federal tax law changes will have on both the CDC and ECD Tax Credits.

IV. Presentation on Property Tax Revenue Divisions for Urban Renewal Areas (TIF)

Dr. Tony Girardi, IDR, Ms. Carrie Johnson, Department of Management (DOM), and Mr. Ted Nellesen, DOM, provided an update and compliance report to the committee on the urban renewal area (also known as tax increment financing or TIF) reporting requirements enacted by the General Assembly in 2012.

Dr. Girardi provided background information on Iowa's urban renewal law and a description of his ongoing research into the efficacy of TIF. He gave a brief overview of how TIF works and the history of TIF in Iowa. Dr. Girardi described the use of TIF in other states and noted differences with Iowa's TIF law. Currently, 49 states and the District of Columbia allow the use of TIF. Of those 49 states, 36 reference blight as a prerequisite or allowable condition for the establishment of a TIF district, three states require a finding of blight prior to the establishment of a TIF, 15 states require that TIF meet a "but for" test, 32 states (including Iowa) allow TIF financing through general obligation bonds, and 14 states provide some type of exclusion from TIF for overlapping school districts.

From 2000-2017, TIF incremental valuation in Iowa has risen from approximately $4.5 billion to $11.4 billion. The majority of this incremental valuation belongs to the commercial property class, followed by residential, industrial, multi-residential, and agricultural. In 2017, 25 percent of industrial property is in a TIF district. The majority of this incremental valuation relates to TIF for economic development. From 1980-2017, property tax revenues dedicated to TIF have increased from approximately $2.7 million to approximately $348.8 million. Of the total property taxes collected during that same period, the percentage collected in TIF districts has increased from approximately 0.1 percent of the total revenues to 5.9 percent of the total revenues. Dr. Girardi gave a brief overview of how TIF impacts school funding and the school aid formula. From 2001-2017, school district property tax revenues diverted to TIF districts have almost doubled, and this increase has produced a corresponding increase in the amount of state aid to school districts. Dr. Girardi provided information relating to TIF valuation by individual counties over the last 17 years.

While noting the limited research on TIF, Dr. Girardi assessed the economic effects of TIF through Iowa's urban core-based statistical areas to analyze whether TIF leads to economic growth. He presented data related to total revenue for fiscal years 2002-2017, and changes in employment and aggregate wages during the same time period. Dr. Girardi concluded that there is no correlation between TIF and economic growth, except for a slight correlation between TIF and industrial concentration. Dr. Girardi noted that the size of a metropolitan area and the educational background of the workforce have more of an impact on economic growth.

Discussion. Committee members discussed the lack of correlation between TIF and economic growth, and the statewide cost of TIF due to the state replacing a certain amount of school aid revenue that is diverted to TIF development. The members discussed the findings relating to industrial TIF districts and economic growth. The members discussed the fact the data presented by Dr. Girardi did not include rural Iowa. The committee members also discussed whether TIF provides enough incentives to change behaviors.

Annual Urban Renewal Report. Ms. Johnson and Mr. Nellesen provided an update to the committee on the Annual Urban Renewal Report (AURR). The update included the types of data submitted by cities and counties, the AURR searchable database, TIF use by cities and counties, TIF projects by type and year, TIF debt balance by type, number of TIF debts by type, annual appropriations to pay off TIF debt, number of TIF debts due to be paid in full, and TIF taxing districts' ending cash balances.

Discussion. Committee members discussed that more commercial projects are in TIF districts than industrial projects, and based on Dr. Girardi's presentation, there may be some benefit to placing more emphasis on industrial projects.

V. Review of Redevelopment Tax Credits

Mr. Matt Rassmussen, Iowa Economic Development Authority (IEDA), presented a report to the committee detailing the Redevelopment Tax Credit Program for Brownfields and Grayfields which provides an investment tax credit for redevelopment projects in Iowa that meet the definition of either a brownfield or grayfield site.

A "brownfield" site includes an abandoned, idled, or underutilized industrial or commercial facility where expansion or redevelopment is complicated by real or perceived environmental contamination. A "grayfield" site includes an industrial or commercial property that is at least 25 years old and that meets one of several conditions relating to vacancy, assessed value, use, or improvements on the property.

Under the program, an owner's equity investment in a grayfield project can receive a tax credit of up to 12 percent of the qualifying investment, or up to 15 percent of the qualifying investment if the project meets the requirements of a green development. A brownfield project can receive a tax credit of up to 24 percent of the qualifying investment, or up to 30 percent of the qualifying investment if the project meets the requirements of a green development. "Qualifying investment" means costs that are directly related to a qualifying redevelopment project and that are incurred after the project has been registered and approved by the IEDA Board, and includes the purchase price, the cleanup cost, and the redevelopment costs.

Mr. Rassmussen provided a history of the program in Iowa. The program was enacted in 2008 with a $1 million statewide program cap and a per project cap of 10 percent of the total credits ($100,000). In 2011, the statewide program cap was raised to $5 million, an independent audit of projects was required, and an automatic program sunset date of June 30, 2021, was established. In 2013, the statewide program cap was raised to $10 million. In 2014, an annual application period was established and the application process was changed from first-come, first-served to competitive scoring.

Mr. Rassmussen detailed the application and review process and provided examples of how the program is being utilized throughout the state. Program applications are accepted annually from July 1 through September 1. The applications are scored and ranked by the Brownfield Advisory Committee based on financial need, feasibility, and the overall quality of the project. A recommendation is then made by the committee to the IEDA Board. If an applicant receives an award, the applicant enters into a contract with the IEDA for completion of the project. With some exceptions, a project must be completed in 30 months. After the project is complete, a claim including a cost certification by an independent Iowa CPA is submitted to IEDA, a site visit is performed, and a tax credit certificate is issued upon compliance with the terms of the contract.

If an applicant does not receive an award, the applicant receives 25 bonus points toward the applicant's competitive score if the applicant reapplies the following year. The award of 25 bonus points on the applicant's competitive score has caused some concern relating to applicants applying a year before the applicant's project is ready in order to receive the bonus points if the applicant reapplies the following year. IEDA has proposed a rule to modify the awarding of bonus points if an application is denied the previous year.

Mr. Zhong Jin, IDR, provided background information and statistical analysis of the Brownfield and Grayfield Redevelopment Tax Credit Program and discussed other states' redevelopment tax credit programs. Eight states, including Iowa, have established tax credit programs dedicated to the cleanup and redevelopment of brownfield or polluted properties. Among the states, Missouri has the highest brownfield tax credit rate at 100 percent and is the only state that requires an applicant to create jobs. New York and Iowa are the only two states that offer a refundable credit. Iowa, Florida, Massachusetts, and Missouri offer transferable credits.

Mr. Jin detailed the amount of redevelopment tax credit awards issued and the percentage of those awards that were transferred from fiscal years 2010-2017. During that time, $31 million in awards were issued to 78 completed projects. Of those awards, $30.6 million were transferable, and $0.32 million were refundable and nontransferable. Eighty-one percent ($24.9 million) of transferable awards have been transferred. Data from the last three years indicates awardees receive 93 cents on the dollar in the transfer process. Also, 204 tax credit claims were made between fiscal years 2010-2017 from which a total of $21,323,880 in credits were applied to tax liabilities and a total of $5,432,449 in credits were carried forward to future tax years. Of the tax credit claims, 14 percent were claimed against individual income tax, 30 percent were claimed against the franchise tax, 36 percent were claimed against the insurance premium tax, and 17 percent were claimed against corporate tax.

Mr. Jin discussed the positive impact redevelopment has on neighborhood property values. Mr. Jin analyzed the Redevelopment Tax Credit Program and the investment impact of the program by examining properties on applications and the wait list between fiscal years 2012-2017. Mr. Jin's analysis of the impact of the award process showed that of 71 properties that were put on the wait list that did not reapply, 22 were redeveloped without a redevelopment tax credit award. Of 26 properties that were put on the wait list, reapplied, and put on the wait list a second time, 18 were redeveloped without a redevelopment tax credit award.

Mr. Jin concluded that properties that have been allocated a redevelopment tax credit award are more likely to be redeveloped, but applicants that have a strong commitment to redeveloping properties are more likely to reapply for awards and proceed with development even if the applicant is not ultimately allocated a redevelopment tax credit award.

Discussion. The committee engaged in a discussion of the Redevelopment Tax Credit Program, including whether many of the projects undertaken as part of the program would have occurred without the tax credit assistance provided by the program. It was noted, however, that it would be difficult to determine whether the property would be redeveloped without the tax credit assistance provided by the program. Committee members also discussed the number of credits that are transferred and if the credits should be refundable instead. The committee further discussed applicants applying just to receive the 25 bonus points toward the applicant's competitive score when reapplying the following year.

VI. Review of the Endow Iowa Tax Credits

Ms. Nichole Hansen, IEDA, provided an overview of the Endow Iowa Tax Credit Program. The Endow Iowa Tax Credit was established in 2003 as a charitable giving incentive program administered by the IEDA to encourage individuals, businesses, and organizations to make investments in their communities through contributions to Endow Iowa qualified community foundations which are tax-exempt, nonprofit, publicly supported philanthropic organizations. The Endow Iowa Tax Credit is a 25 percent tax credit available to all Iowa taxpayers who make a qualifying charitable donation. IEDA awards the credits on a first-come, first-served basis. Community foundations apply to IEDA on behalf of their donors to receive tax credits. IEDA awards tax credits on an ongoing basis until the annual cap of $6 million is reached. Once the annual cap is reached, IEDA adds donors to a wait list to receive tax credits in the following year.

To qualify, donations must be made to a qualified community foundation established for the benefit of an Iowa charitable purpose. Donations may be of any size, however, tax credits granted to a single taxpayer cannot exceed $300,000 annually. Ten percent of the annual $6 million cap is reserved for donations under $30,000 to ensure smaller donors receive credits. In 2018, 33 percent of all donations fell into the small donor category. The average donation is $6,900. Credits are nonrefundable but may be carried forward for up to five years. Credits may be claimed against state corporate income, individual income, franchise, insurance premium, and moneys and credits taxes.

Ms. Hansen stated that the Endow Iowa Tax Credit Program continues to see high demand. Currently, only $900,000 of the $6 million of authorized credits remain available for the remainder of 2019.

In 2018, Endow Iowa Tax Credits leveraged approximately $24 million in donations. Iowa's qualified community foundations reported a 6.89 percent growth in permanent endowment assets in 2017.

Ms. Angela Gullickson, IDR, provided background information and statistical analysis of the Endow Iowa Tax Credit Program. Ms. Gullickson also provided information on similar programs in other states. Apart from Iowa, only Kentucky, Montana, and North Dakota offer similar tax credits, and since 2013, only Maryland has added this type of credit. The tax credit is nonrefundable in all four states, and only Kentucky and Maryland allow the donation to be claimed as both a tax credit and an itemized deduction. Montana is the only state that does not allow the credit to be carried forward. Three states, including Iowa, allow the tax credit to be carried forward for five years, and North Dakota allows the tax credit to be carried forward for three years.

Since the inception of the Endow Iowa Tax Credit in 2003, there has been a total of almost $24 million in donations made to Endow Iowa qualified community foundations, with an average donation of $8,789.

As a result of the donations, 35,950 separate Endow Iowa Tax Credit awards have been issued totaling almost $63 million, with an average tax credit award of $1,745.

Ms. Gullickson next provided data on the tax credit awards from years 2006-2017 according to the taxpayer's age, county of residence, persistence of the donor, household adjusted gross income (AGI), timing, and other measurements. The average donor is more than 55 years of age. There were 10,409 taxpayers who made donations, 62.7 percent of whom were one-time donors. During this period of time, 3,885 taxpayers made donations in more than one year, and 15 taxpayers donated each year. Information was also provided on the distribution of tax credits awarded according to household adjusted gross income. Ms. Gullickson noted that less than 2 percent of tax credit awards went to households with an AGI of $1 million or more. When the Endow Iowa Tax Credits are analyzed according to the time frame in which the tax credits were claimed, 75.44 percent of credits were claimed within the first two years of issuance, and the percentage claimed declined dramatically in years three through five. An average of 13.61 percent of tax credits remain unclaimed. Ms. Gullickson concluded her presentation by providing data on taxpayers with tax credit award amounts that are greater than the tax liability of the taxpayer for award years 2006-2012. During this period, 512 taxpayers received tax credit awards that exceeded the taxpayer's tax liability and 428 taxpayers with zero tax liability also received tax credit awards.

Discussion. The committee discussed unclaimed awards going back into the general fund. The committee also discussed the possibility that people will make contributions even without the Endow Iowa Tax Credit. There was also discussion regarding if it might be beneficial to focus on smaller donations. However, Ms. Gullickson noted that when Michigan repealed a tax credit similar to the Endow Iowa Tax Credit, a significant drop in small donations occurred.

VII. Tax Credit Update

Ms. Amy Harris, IDR, presented information on tax credits that the Tax Expenditure Committee is not required to review pursuant to Iowa Code section 2.48. She noted that IDR is releasing fact sheets on the following tax credits: the Adoption Tax Credit; Biodiesel Blended Fuel Tax Credit; E15 Plus Gasoline Promotion Tax Credit; E85 Gasoline Promotion Tax Credit; Farm to Food Donation Tax Credit; School Tuition Organization Tax Credit; Solar Energy System Tax Credit; Volunteer Firefighter and Emergency Medical Services Personnel and Reserve Peace Officer Tax Credit; and the Workforce Housing Tax Incentive Program. Ms. Harris noted the Geothermal Heat Pump Tax Credit was repealed beginning on January 1, 2019.

Ms. Harris provided the committee with facts about some of the tax credits. Seventy-eight percent of eligible taxpayers claim the Volunteer Firefighter and Emergency Medical Services Personnel and Reserve Peace Officer Tax Credit. The Solar Energy System Tax Credit is highly oversubscribed, with 89 percent of the $5 million cap in 2018 being awarded for 2017 projects. The Farm to Food Donation Tax Credit is the most underutilized tax credit, with only 39 taxpayers receiving a tax credit award between years 2014-2017, and only 10 of 65 registered food banks receiving eligible donations between years 2014-2017. The Adoption Tax Credit is a refundable tax credit for up to $5,000 of qualified adoption expenses. Ms. Harris did note that IDR may propose a change to the Adoption Tax Credit allowing for any qualified adoption expenses occurring over multiple tax years to be claimed in a single tax year.

Ms. Harris also noted the largest tax credit not required to be reviewed by the Tax Expenditure Committee is the Workforce Housing Tax Incentive Program used for incentivizing Iowa housing projects. The Workforce Housing Tax Incentive Program is highly oversubscribed with 120 projects totaling $53 million in tax credits on the wait list at this time. This tax credit program is the remaining program targeting building investment that has a first-come, first-served tax credit allocation process.

Ms. Harris also discussed the E15 Plus Gasoline Promotion Tax Credit and the potential impact of 2019 policy issues. Ms. Harris presented information on federal tax law changes and the impact on charitable contributions. Iowa has three tax credits potentially impacted, including the School Tuition Organization Tax Credit, the Charitable Conservation Contribution Tax Credit, and the Endow Iowa Tax Credit.

Finally, Ms. Harris discussed the Tax Credit Award, Claim, and Transfer Administration System (CACTAS) which uses real-time consistent award data to update tax credit forecasts, allows more detailed evaluations and fiscal estimates, and is used to meet GASB 77 requirements in annual state and local reports. A majority of tax credit applications have been developed in CACTAS.

Discussion. The committee had a short discussion regarding the number of tax credits available in Iowa. There was a short discussion on whether the Workforce Housing Tax Incentive Program should be changed to a competitive scored application process rather than a first-come, first-served application process.

VIII. Public Comment and Committee Discussion

During the public comment period of the meeting, no members of the public addressed the committee. The committee briefly discussed the presentations made during the meeting, the importance of the committee going forward, and that an interim committee is going to review all tax credits in 2019.

IX. Materials Filed With the Legislative Services Agency

The following materials listed were distributed at or in connection with the meeting and are filed with the Legislative Services Agency. The materials may be accessed from the link on the committee's website: www.legis.iowa.gov/committees/meetings/documents?committee=594&ga=87

1. Agenda
2. Child and Dependent Care and Early Childhood Development Tax Credits, Iowa Department of Revenue
3. Property Tax Increment Financing, Iowa Department of Revenue
4. Annual Urban Renewal Report, Iowa Department of Management
5. Redevelopment Tax Credit Program for Brownfields and Grayfields, Economic Development Authority
6. Redevelopment Tax Credit, Iowa Department of Revenue
7. Endow Iowa Tax Credit Program, Economic Development Authority
8. Tax Credit Updates, Iowa Department of Revenue
9. Adoption Tax Credit, Iowa Department of Revenue
10. Biodiesel Blended Fuel Tax Credit, Iowa Department of Revenue
11. E15 Plus Gasoline Promotion Tax Credit, Iowa Department of Revenue
12. E85 Gasoline Promotion Tax Credit, Iowa Department of Revenue
13. Farm to Food Donation Tax Credit, Iowa Department of Revenue
14. Redevelopment Tax Credit, Iowa Department of Revenue
15. School Tuition Organization Tax Credit, Iowa Department of Revenue

16. Solar Energy System Tax Credit, Iowa Department of Revenue
17. Tuition and Textbook Tax Credit, Iowa Department of Revenue
18. Volunteer Firefighter and Emergency Medical Services Personnel and Reserve Peace Officer Tax Credit, Iowa Department of Revenue