PENNSYLVANIA

RURAL JOBS AND INVESTMENT TAX CREDIT

An Evaluation of Program Performance

January 2023

COMMONWEALTH OF PENNSYLVANIA
INDEPENDENT FISCAL OFFICE

Independent Fiscal Office
Rachel Carson State Office Building
400 Market Street
Harrisburg, PA 17105

717-230-8293 | contact@ifo.state.pa.us | www.ifo.state.pa.us

Staff Acknowledgements

Robyn Toth, Fiscal Analyst/Communications
Mitchell Young, Revenue Analyst I

Staff Contact: rtoth@ifo.state.pa.us

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INDEPENDENT FISCAL OFFICE

January 3, 2023

The Honorable Members of the Performance-Based Budget Board and Chairs of the House and Senate Finance Committees:

Act 48 of 2017 requires the Independent Fiscal Office (IFO) to review various state tax credits over a five-year period. For the fifth year, the IFO reviewed four tax credits: Manufacturing, Resource Manufacturing, Rural Jobs and Investment, and Waterfront Development Tax Credits. The act requires the IFO to submit tax credit reviews to the Performance-Based Budget Board and the Chairs of the House and Senate Finance Committees and to make reports available to the public on the IFO website.

This report contains the tax credit review for the Rural Jobs and Investment Tax Credit (RJITC). The IFO identified similar programs in other states, reviewed available research, held discussions with various stakeholders and met with agency staff who administer the tax credit. Based on that research, the IFO submits this report to fulfill the requirements contained in Act 48.

Seventeen states (including Pennsylvania) offer investment programs similar to the RJITC. Eight states offer incentives in the form of a tax credit equal to 39% of the qualified investment, eight states offer a tax credit equal to another amount (24% to 100%) and one state (Alaska) offers a loan program. All states limit the dollar amount of incentives awarded each year, although not necessarily through the use of an annual cap. Allocations range from $6 million (Pennsylvania) to $40 million (Alaska) annually. This analysis examined available data and other issues that determine the effectiveness of the RJITC Program.

The IFO welcomes all questions and comments on the contents of this report. Questions and comments can be sent to contact@ifo.state.pa.us.

Sincerely,

Matthew J. Knittel

Dr. Matthew J. Knittel
Director

Rachel Carson State Office Building, 400 Market Street, Harrisburg PA 17105
www.ifo.state.pa.us | (717) 230-8293 | contact@ifo.state.pa.us

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General Findings and Recommendations

Enacted in 2016, the Rural Jobs and Investment Tax Credit (RJITC) is administered by the Department of Community and Economic Development (DCED). Under the program, approved rural growth funds are provided up to $50 million in investment authority, with 60% of that authority (maximum of $30 million) authorized as credit-eligible contributions. When an approved investor contributes credit-eligible capital to an approved fund, the investor (1) receives an equity interest in the fund or a debt instrument with a minimum of a five-year maturity and (2) qualifies for a tax credit equal to 100% of the credit-eligible investment. The contribution made by the business firm must be used by the rural growth fund for investment in rural growth businesses. The RJITC Program is currently capped at an aggregate of $30 million, with $6 million awarded annually over a five-year period (20% available in each year).

The **general findings** of this report are as follows:

- The first rural growth funds were approved in 2021, when DCED approved four funds with a total investment authority of $50 million ($12.5 million each), $30 million of which ($7.5 million each) represented credit-eligible capital contributions.
- The funds have up to three years from the closing date to invest in approved rural businesses. According to the latest data available, three funds provided $7.3 million in capital to four rural businesses located in Adams, Berks, Luzerne and Mercer counties. According to filed reports, 106 jobs have been created or retained due to the program.
- Because the RJITC is still in the early stages of the program, the IFO does not have sufficient data to compute an economic impact or return on investment (ROI).
- Evaluations of similar programs in other states find concerns regarding program effectiveness and efficiency.
- Rural growth funds have an incentive to engage in investments that provide the highest economic return for their investors instead of those that provide the greatest benefit to state residents.
- The tax credit provides significant benefits for the funds, even if they must repay some portion of the tax credits upon exit from the program. For example, the funds raised $50 million to invest in rural businesses (typically loans) for seven years. The funds receive $30 million in tax credit authority under the program and repayment of the $50 million in loans (or equivalent equity), plus interest and fees.

The final section of this report contains various **recommendations**. A summary is as follows:

- This program would be more effective as a loan program administered by DCED.
- Additional funds should not be allocated until the impact of the initial $30 million in tax credits can be fully assessed.

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Introduction

Act 48 of 2017 requires the Independent Fiscal Office (IFO) to review various state tax credits over a five-year period.[1] For the fifth year, the IFO reviewed four tax credits: Manufacturing, Resource Manufacturing, Rural Jobs and Investment, and Waterfront Development Tax Credits. The act requires the IFO to submit tax credit reviews to the Performance-Based Budget Board and the Chairs of the House and Senate Finance Committees and to make reports available to the public on the IFO website.

The act specifies that tax credit reviews shall contain the following content:

- The purpose for which the tax credit was created.
- Whether the tax credit is accomplishing its legislative intent.
- Whether the tax credit could be more efficiently implemented through other methods.
- Any alternative methods which would make the tax credit more efficient.
- The costs to provide the tax credit, including the administrative costs to the Commonwealth and local government entities within this Commonwealth.

The act also specifies that the IFO shall develop a tax credit plan for all tax credits subject to review. The plans should include performance measures, and where applicable, the measures should reflect outcome-based measures (including efficiency measures), measures of status improvements of recipient populations, and economic outcomes or performance benchmarks against similar state programs or similar programs of other states or jurisdictions. The IFO submits this report to fulfill these requirements for the Rural Jobs and Investment Tax Credit.

The remainder of this review contains three sections. **Section 2** discusses how the tax credit is administered and presents historical data. **Section 3** presents relevant data for states that offer programs similar to Pennsylvania's Rural Jobs and Investment Tax Credit and an overview of available research. **Section 4** concludes with the tax credit plan, as required by Act 48. An economic impact of the program is excluded from the analysis because the program is still in the early stages and outcome data are incomplete. A list of reports, studies and data sources used for this report can be found in the **Appendix**. If submitted, written comments provided by stakeholders and affected agencies are included in the Appendix.

[1] Act 48 of 2017 is also known as the Performance-Based Budgeting and Tax Credit Efficiency Act. See the Appendix for the Tax Credit Review Schedule.

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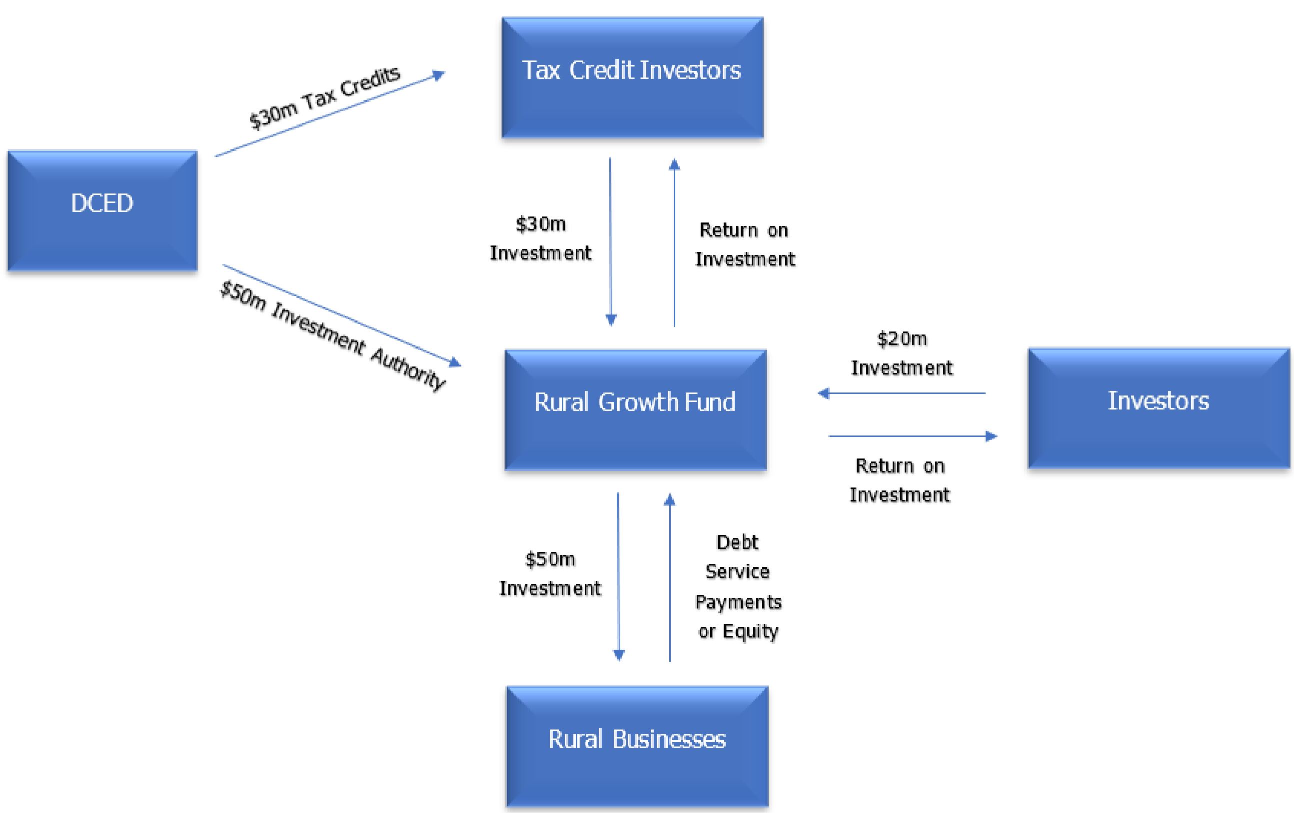
Rural Jobs and Investment Tax Credit Overview

Article XVIII-G of the Tax Reform Code of 1971 (Act 84 of 2016) created the Rural Jobs and Investment Tax Credit (RJITC) Program. Under the program, DCED may grant approved rural growth funds up to $50 million in investment authority, with 60% of that authority (maximum of $30 million) authorized as credit-eligible contributions. When an approved investor (i.e., qualified business firm) contributes credit-eligible capital to an approved rural growth fund, the investor receives (1) an equity interest in the fund or a debt instrument with a minimum of a five-year maturity and (2) qualifies for a tax credit equal to 100% of the credit-eligible investment. The contribution made by the business firm must be used by the rural growth fund for investment in rural growth businesses. Any credits issued under the RJITC Program may be rescinded or recaptured if the rural growth fund fails to comply with program requirements. The flow of funds for the RJITC is outlined in **Figure 2.1**.

Figure 2.1

RJITC Flow of Funds



The RJITC Program is currently capped at an aggregate amount of $30 million, with $6 million awarded annually over a five-year period (20% available in each year) and DCED may issue recaptured or unissued credits from prior fiscal years.[2] The earliest tax credits could be awarded was fiscal year (FY) 2021-22 but none were awarded in that year. Credits cannot be utilized in the first three years after award (i.e., credits can be claimed in the taxable years that include the third through seventh anniversary of the closing date of the fund).[3]

Tax credits may be used to offset up to 100% of a firm's bank and trust company shares, title insurance company shares, insurance premiums tax (including surplus lines and retaliatory tax), and mutual thrift institutions tax liabilities. Credits not used in the tax year that the credit is first available may be carried forward five years or until the expiration of the tax credit. The tax credit is non-refundable, may not be carried back to preceding tax years and can only be sold to affiliated companies.

The RJITC eligibility requirements vary by participant. The text that follows provides an overview.

Qualified Business Firms

A qualified business firm (tax credit investors in Figure 2.1) must be registered to do business in Pennsylvania and subject to the bank and trust company shares, title insurance company shares, insurance premiums or mutual thrift institutions tax. Firms must also remain in compliance with Pennsylvania laws and regulations.

Rural Growth Funds

Qualified rural growth funds are designated to receive up to $50 million in capital contributions and credit-eligible contributions (credit-eligible contributions are capped at 60%, or $30 million of total capital contributions). The fund has three years after it collects the capital contributions to invest the funds in approved rural businesses.

Applicants must meet the following criteria to apply for rural growth fund designation:

- Be a licensed rural business investment company under the Consolidated Farm and Rural Development Act or a small business investment company under the Small Business Investment Act.
- Have invested at least $100 million in nonpublic companies located in rural areas of the Commonwealth or other states prior to the application date.
- Have at least one principal who has been an officer or employee of the applicant for at least four years prior to the application date.
- Be registered to do business in the Commonwealth and subject to Pennsylvania taxes.

Rural Businesses

Rural businesses work directly with the rural growth funds and not DCED. In order to qualify for an investment from a rural growth fund, the rural business must meet the following criteria:

[2] In part, Act 13 of 2019 increased the annual program cap from $1 million to $6 million and the aggregate cap from $6 million to $30 million.
[3] The closing date is defined as the date that the rural growth fund collected all of the credit-eligible capital contributions and capital contributions as specified in Section IV of the Program Guidelines.

- Have fewer than 150 employees and not more than $15 million in net income for the preceding calendar year.
- Have principal business operations in one or more rural areas of the state.[4]
- Engage in industries related to manufacturing, plant sciences, services or technology. If the business is not engaged in one of those sectors, DCED can make an exception if the investment will be highly beneficial to the economic growth of the state.

The subsections that follow list the goals and purpose of the tax credit, discuss the application process and administration of the tax credit, and conclude with a presentation of program data.

Goals and Purpose

Act 48 of 2017 requires that all tax credit reviews published by the IFO shall discuss (1) the purpose for which the tax credit was created and (2) whether the tax credit is accomplishing its legislative intent. For this credit, the IFO reviewed documentation provided by the Department of Revenue (DOR), DCED and the authorizing legislation for the RJITC. For this review, the IFO established the goals and purpose of the RJITC Program as follows:

Goals

- Stimulate business development in rural areas.
- Retain and attract new rural businesses and industry to the Commonwealth.
- Create family-sustaining rural jobs.

Purpose

- Stimulate economic growth and job creation in rural areas by providing rural business owners, who may otherwise have difficulty obtaining investment, with increased access to capital for business development.

Administration

DCED administers the RJITC and reviews applications. The text that follows is a summary of the approval process and reporting requirements for rural growth funds, qualified business firms (i.e., investors) and rural businesses.[5]

Approval Process

Rural Growth Funds

Investment companies that apply for rural growth fund designation must submit the following to DCED via email and mail:

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[4] See "Rural Jobs and Investment Tax Credit: Program Guidelines," Pennsylvania Department of Community and Economic Development (September 2020) for rural business determination.
[5] See "Rural Jobs and Investment Tax Credit: Program Guidelines," Pennsylvania Department of Community and Economic Development (September 2020).

1. Total investment authority requested.
2. Documents that verify the following:
    a) The applicant (or affiliates) is licensed as a rural business investment company or as a small business investment company.
    b) The applicant (or affiliates) has invested at least $100 million in nonpublic companies located in rural areas of the Commonwealth or in other states.
    c) An estimate of the number of jobs to be created or retained in the Commonwealth that will result from the applicant's rural growth investments.
    d) At least one principal has been an officer or employee of the applicant or affiliate of the applicant for at least four years prior to the date of application under the program.
    e) A 10-year business plan that projects state and local tax revenue generated by prospective rural growth investments.
    f) A signed affidavit from each investor stating the amount of credit-eligible capital contribution commitments made by each business firm.
    g) A minimum of five references consisting of two to three investors and two to three portfolio company representatives.
    h) A $500 non-refundable application fee.

DCED approves or denies applications within 60 days of receipt. The allocation of investment authority is made in the order in which approved applications are received. If requests for investment authority exceed $50 million, DCED will reduce the investment authority and credit-eligible contributions for each approved application proportionally based upon the amount of investment authority sought in each approved application.

If approved, rural growth fund applicants will be notified of (1) the amount of the rural growth fund's investment authority under the program and (2) the amount of credit-eligible capital contributions allocated to each business firm which submitted the required affidavit. Credit-eligible contributions shall comprise 60% of a growth fund's investment authority. Notifications are sent to the approved fund via email. If DCED denies an application, the applicant may resubmit the application within 30 days after the notification.

The rural growth fund must collect the following within 60 days of approval from DCED:

- Credit-eligible capital contributions from each business firm.
- Investments of cash that when combined with the credit-eligible capital contributions equal the rural growth fund's investment authority. At least 10% of the rural growth fund's investment authority shall be comprised of equity investments contributed by affiliates of the fund, including employees, officers, and directors of the affiliates.

The rural growth fund must provide DCED with documentation that all contributions have been collected within 65 days of approval. The fund must also submit to DCED for approval a completed Credit-Eligible Capital Contribution Request Form for each credit-eligible contributing business firm. Upon approval of the credit-eligible contribution, a letter is issued indicating the approved contribution amount. Business firms must submit this letter with their tax credit application.

The rural growth fund is required to maintain accurate records of investor contributions and expenditure of those contributions until the fund successfully exits the program.[6] If the rural growth fund fails to meet program requirements, its approval and designation will be revoked. The associated investment authority and credit-eligible capital contributions will be reallocated.[7]

Qualified Business Firms

Business firms that make credit-eligible contributions must submit a Rural Jobs and Investment Tax Credit Application no later than February 1 for contributions approved in the preceding calendar year.[8] DCED processes applications within 30 days of receipt and notifies the applicant of approval or denial. If approved, tax credit certificates are awarded by April 1 of the first year the tax credit is eligible to be utilized.

DOR evaluates all applications for state tax compliance. Applications considered noncompliant are not eligible for the credit, unless the applicant resolves the issue within the timeframe set by DOR.

Tax credit certificates will be rescinded if any of the following occur before the rural growth fund exits the program:

- The rural growth fund does not invest all its investment authority in rural growth investments in the Commonwealth within three years of the closing date.
- The fund does not invest at least 25% of its investment authority in rural businesses engaged in manufacturing within three years of the closing date.
- The fund fails to maintain rural growth investments totaling 100% of its investment authority until the seventh anniversary of the closing date.
- The fund makes a distribution or payment that results in the fund having less than 100% of its investment authority in rural growth investments in Pennsylvania or available for investments in rural businesses and held in cash or market securities.
- The fund invests more than 20% of its investment authority, exclusive of receipts or redeemed rural growth investments, in the same rural business, including amounts invested in affiliates of the rural business.
- The fund makes a rural growth investment in a rural business that, directly or indirectly through an affiliate, owns, has the right to acquire an ownership interest, makes a loan to, or makes an investment in the rural growth fund, an affiliate of the rural growth fund, or a business firm in the rural growth fund. This does not apply to investment in publicly-traded securities by a rural business or an owner of an affiliate of a rural business.

DCED will notify the fund if the conditions are not met, and the fund will have 90 days from the notification date to correct any violation. Tax credit certificates will be revoked if the violation has not been corrected within the given timeframe.

DCED will first reallocate the investment authority to rural growth funds that were awarded less than the requested investment authority in their applications. If investment authority remains after the reallocation,

[6] Funds may exit the program after seven years.
[7] See Program Guidelines for the full list of Rural Growth Fund Requirements.
[8] To qualify for the tax credit, credit-eligible capital contributions made by the business firm to a rural growth fund must be used by the fund for rural growth investments in a rural business.

the remaining portion may be awarded to new applicants.

Reporting Requirements

Rural Growth Funds

Rural growth funds must submit a report on or before the fifth business day after the second anniversary of the closing date. The report must provide documentation of rural growth investments and include the following:

- A bank statement that itemizes each rural growth investment.
- A completed Initial Report for each rural growth investment. The report must include the name, location, size, and industry of each rural business.
- A copy of the commitment letter or summary of the terms and conditions of each rural growth investment accepted by the rural businesses.

Rural growth funds are also required to submit an Annual Report no later than March 1 of each year following the closing date. The report updates the documentation contained in the Initial Report regarding:

- Number of jobs created and retained by each rural business.[9]
- Average hourly wage of the jobs reported.
- Any rural growth investments that were sold or repaid during the prior calendar year.
- An updated Initial Report for any new rural growth investments made during the previous calendar year.

The first Annual Reports were submitted in March 2022. Rural growth funds have until 2024 to distribute all funds to rural businesses (three years from the closing date). Therefore, the Annual Reports released in March 2022 do not contain complete information on rural growth investments.

Rural Businesses

Each rural business that receives a rural growth investment must file a Rural Business Report by March 1 following the submission of the rural growth fund's Initial Report. The report must include:

- Number of jobs existing at the rural business prior to the rural growth investment.
- Number of new jobs created because of rural growth investment.
- Number of jobs retained because of rural growth investment.

The rural business report is evaluated by DCED and DOR for compliance. Failure to submit the report may result in the reduction of investment authority or credit-eligible capital contribution authority of the rural growth fund.

[9] The jobs must have been created by the rural business, pay at least 150% of the federal or state minimum wage (whichever is greater), and not located in the state at the time of the initial investment. The jobs retained must have existed in the state prior to the initial investment, pay at least 150% of the federal or state minimum wage (whichever is greater), and would have been lost or moved out of the state without the rural growth investment. See program guidelines for instructions on calculating the number of jobs created and the number of jobs retained.

The estimated annual staff time and cost for DCED and DOR to administer the RJITC are currently nominal, but those costs are expected to increase as credits are awarded.

Historical Data

Rural Growth Funds

The program had a total of five rural growth fund applicants, four of which were approved. Requests for investment authority exceeded the program limit, so amounts were proportionally reduced. DCED awarded $12.5 million in total investment authority to each fund, with $7.5 million of that amount available as credit-eligible capital contributions. (See **Table 2.1**.) Based on data received from DCED on August 3, 2022, $7.3 million of those funds had been invested in rural businesses.

Table 2.1
Rural Growth Funds

Rural Growth Fund	Credit-Eligible Authority	Total Investment Authority	Investment Deployed[1]
Advantage Capital Pennsylvania Partners	$7.5	$12.5	$3.5
Enhanced Capital Pennsylvania Rural Fund	7.5	12.5	1.3
Stonehenge Capital Fund Pennsylvania	7.5	12.5	2.5
PA Rural Jobs Subsidiary Fund	7.5	12.5	0.0
Total	**30.0**	**50.0**	**7.3**

Notes: Millions of dollars.

1 Based on data received August 3, 2022. Funds have until 2024 to deploy all of the capital.
Source: Department of Community and Economic Development.

A rural growth fund may exit the program after the seventh anniversary of the closing date by completing a Rural Jobs and Investment Tax Credit Exit Application. The rural growth fund must calculate any state repayment amount due as part of the exit application.[10] The rural growth fund must remit the state repayment amount due before it can make a distribution or payment exceeding any business firm's investment authority. The exit will be approved as long as no tax credit certificates have been rescinded and no notices of revocation remain unprocessed. DCED will provide written notification if the exit request is denied. The first year that approved rural growth funds will be eligible to exit the program is 2028. Based on the data in Table 2.1, investments by each rural growth fund need to generate 250 new or retained jobs (250 x $30,000 = $7.5 million in credit eligible contributions) to avoid a state repayment.

Rural Businesses

The rural growth funds have until 2024 to invest $50 million in approved rural businesses. Each fund cannot invest more than 20% of its investment authority in the same rural business. Investments can be in the form of equity or debt with a stated maturity date of at least one year after the date of issuance. To qualify as a rural growth investment, the rural business must submit documentation to the rural growth fund

[10] A state repayment is due if the rural growth fund's credit-eligible capital contributions exceed the product obtained by multiplying $30,000 by the number of jobs created or retained as reported in the fund's annual reports.

stating they were denied similar financing from a commercial bank for a secured loan or revolving line of credit. The rural growth fund assumes the responsibilities and the risk associated with the debt or equity investment.

Through 2021, three funds made four investments that total $7.3 million to support businesses in four counties: Adams, Berks, Luzerne and Mercer. The most recent reports indicate that 106 jobs with average wages between $25 to $32 per hour or an average annual salary of $48,000 have been created or retained due to the program. (See **Table 2.2**.)

Table 2.2
Qualified Investments in Rural Businesses

Rural Growth Fund	Total Investment[1]	# Rural Businesses[2]	# of Jobs[3]	Average Wage	Average Salary
Advantage Capital Pennsylvania Partners	$3.5	2	45	$25/hr	--
Enhanced Capital Pennsylvania Rural Fund	$1.3	1	49	--	$48,000
Stonehenge Capital Fund Pennsylvania	$2.5	1	12	$32/hr	--
PA Rural Jobs Subsidiary Fund	--	--	--	--	--
Total	**$7.3**	**4**	**106**	**--**	**--**

1 Millions of dollars.

2 Number of rural businesses supported by rural growth investments.

3 Number or jobs created or retained.

Source: Department of Community and Economic Development. Based on 2022 Annual Reports.

Tax Credits

DCED authorized $30 million in tax credits (maximum) to seven business applicants (investors in rural growth funds) in FY 2021-22.[11,12] Firms may use 20% of the approved tax credit beginning in the taxable years that include the third, fourth, fifth, sixth, and seventh anniversaries of the closing date. The tax credits will be eligible for utilization beginning in 2024 through 2028. Therefore, no credits have been utilized to date.

Based on the limited data available, it is unclear how many rural businesses will be supported, or the number of jobs created or retained as a result of the program.[13] It is also unknown how much the rural growth funds will receive in repayment, the state repayment amount owed (if any), and any distributions or payments made from the fund to investors, partners and/or affiliates upon exit of the program.

[11] Fiscal year 2021-22 was the first year Rural Jobs and Investment Tax Credits were authorized.
[12] Two investors made credit-eligible capital contributions to two different rural growth funds.
[13] Table 2.2 reflects 106 jobs created or retained as a result of the investments to date. A cost per job is not computed from these data because it is unclear whether the rural businesses have had sufficient time to deploy the invested capital.

State Comparison

The RJITC is similar to the federal New Markets Tax Credit (NMTC) Program. The federal NMTC Program was established in 2000 and was renewed through 2025 for $5 billion in annual investment allocation authority. The goal of the federal NMTC Program is to help economically distressed communities attract private capital by providing investors with federal tax incentives. The Community Development Financial Institutions Fund (CDFI Fund), part of the U.S. Treasury, oversees the program and awards NMTC allocations to approved Community Development Entities (CDEs). CDEs offer tax credits to investors in exchange for equity in the CDE. The investments made in the CDE's are used to finance businesses in underserved low-income communities. Corporate investors can receive a 39% tax credit (taken over seven years) for qualified equity investments made in the CDE.

Many states have developed their own New Markets Tax Credit, or Certified Capital Company (CAPCO) Program, or both, that function similarly to the federal NMTC and the Pennsylvania RJITC. The differences between the programs are generally limited to the type of investment required (e.g., rural, technology focused, economically distressed community, etc.), the share of the investment awarded as a tax credit and the number of years over which credits may be claimed.

Table 3.1 provides details for similar investment programs in other states. A comparison reveals that:

- The type of incentives offered are largely in the form of tax credits, apart from Alaska which offers a loan program. Most states provide a tax credit at a rate equal to 39% of the qualified investment. Eight states offer credits between 24% to 100% of the qualified investment, and Pennsylvania offers the highest rate.
- Some states offer the tax credit on only a portion of the required investment (e.g., Pennsylvania offers a 100% tax credit on $30 million of the required $50 million investment). Other states offer the tax credit on the full amount of the required investment (e.g., Georgia offers a 60% tax credit on the full $100 million investment).
- Most states impose a limit on the amount of capital the rural business can receive from the investment company. Qualified rural businesses in Pennsylvania can receive up to 20% of the rural growth fund's investment authority. Based on the investment authority awarded, the maximum amount a Pennsylvania rural business can receive from a single rural growth fund is $2.5 million. Qualified equity investments in other states range from $2.6 million to $10 million.
- All states limit the dollar amount of incentives awarded each year although not necessarily through the use of an annual cap. Annual allocations range from $6 million (Pennsylvania) to $40 million (Alaska). Pennsylvania's program is currently capped at $30 million, with $6 million in tax credits awarded annually over five years.

Table 3.1
Comparison of State Rural Jobs and Investment Incentives

			Limitations ($ millions)	
State	Credit Rate[1]	Per Business Cap	Investment Authority	Annual Cap
Alabama	50%	$10 million QLICI per qualified active low income community business	--	$20
Alaska[2]	100% guarantee on leverage loans	--	--	$40
Arkansas	58%	--	$166	--
Florida	39%	$10 million in QEI	--	$37
Georgia	60%	Maximum is the greater of 20% of rural fund's capital investment authority or $6.5 million in QEI	$100	$15
Illinois	39%	$10 million in QEI	--	$20
Kentucky	39%	$10 million in QEI	--	$10
Louisiana	45%	$5 million in QEI	$75	--
Maine[3]	39%	$10 million in QEI	$250	$20
Mississippi	24%	$10 million	--	$15
Missouri	39%	$10 million	--	$25
Nebraska	39%	$10 million in QEI	--	$15
Nevada	58%	30% of purchase price of QLICI	$200	$8
Ohio	100%	$15 million	$75	--
Oklahoma	60%	--	$100	$15
Oregon	39%	TC invested in one project can't exceed $8 million	$200	$16
Pennsylvania[4]	**100%**	**No more than 20% of its investment authority in the same rural business**	**$50**	**$6**
Utah[4]	58%	$5 million	$42	--

Note: QLICI is qualified low-income community investment. QEI is qualified equity investment. TC is tax credit.

1 Represents rate applied to qualified investment. Additional investment (not eligible for credit) may be required and included in the investment authority.

2 Alaska is the only loan program displayed in the table.

3 The limit on the qualified low-income community investment increases to $40 million per project if it is constructed, maintained, or operated by a qualified active low-income community business that is a manufacturing or value-added production enterprise.

4 Pennsylvania's program has an aggregate cap of $30 million in tax credits. Utah has a similar aggregate cap of $24.36 million in tax credits.

Source: CCH and various state agency websites.

Literature Review

As part of its analysis, the IFO reviewed studies and reports on the impact of programs similar to the RJITC. The text that follows provides a summary of eight reports. These reports are reviewed to provide context, and the IFO has no opinion or insights regarding the analysis contained therein.

New Markets Tax Credit Progress Report (2022) [14]

The federal NMTC offers a 39% tax credit (claimed over seven years) for qualified investments in Community Development Entities (CDEs). The CDEs use the proceeds of equity investments to provide low-cost capital to eligible communities. CDEs are organizations with a track record of providing capital to underserved areas. The Community Development Financial Institutions (CDFI) Fund within the U.S. Department of Treasury administers the program, awards the NMTC allocation to CDEs and tracks compliance. The NMTC was initially authorized from 2001 through 2007 but has been extended numerous times. Most recently, the tax credit was extended through 2025 at $5 billion in annual allocation authority.

According to the NMTC Coalition's latest federal progress report, 277 projects totaling $6.1 billion received $3.2 billion in NMTC distributions in 2021. The projects created approximately 53,000 jobs with a federal cost per job averaging $15,000. Projects that received NMTC allocations were located across 47 states and territories and 31% of the financing went to non-metropolitan counties. NMTC distributions supported manufacturing and industrial businesses, real estate construction and renovation projects and healthcare related projects.

A Limited Review of the Utah Rural Jobs Act (2021) [15]

The Office of the Legislative Auditor General performed an audit of the Utah Rural Jobs Act Program in 2021. The Utah Rural Jobs Act authorizes $42 million in investment authority to rural investment companies and Utah Governor's Office of Economic Development can approve up to $24.36 million in tax credits for qualified investors that make a credit-eligible contribution to a rural investment company. The intent of the program is to encourage expansion and development of rural businesses in Utah and eligible small businesses can receive up to $5 million in capital to use for business expansion and development. The tax credit is issued incrementally on the fourth through seventh anniversary of the closing date.

The audit report noted that an ROI could not be determined for the Utah Rural Jobs Act because the current statute was unclear and the office lacked access to relevant tax documents. The review provided an alternate measure, cost of investment per job, by comparing jobs creation to tax credits. The investment cost per job ranged from $22,200 to $41,700 depending on the number of annual jobs included. The lower figure uses the number of new <u>and</u> retained jobs, while the higher figure uses net new jobs only. The report recommends only counting the number of net new annual jobs created. The method used is important because rural investment companies are required to compute a state reimbursement amount upon exit, and the annual jobs figure is part of that calculation. The report also identified the potential for double counting. When two rural investment companies invest in the same small business, the number of new annual jobs created could be counted twice. It was recommended that firms apply an apportionment factor

[14] "New Markets Tax Credit Progress Report," New Markets Tax Credit Coalition (2022).
[15] "A Limited Review of the Utah Rural Jobs Act," Office of the Legislative Auditor General (April 2021).

based on the share of the total investment. Finally, the report recommended that all new program performance metrics should be tied to predefined standards that reflect intended outcomes and that all metrics are timely and include an end date.

Fiscal Impact of the Georgia Rural Jobs Tax Credit (2020)[16]

The Georgia Agribusiness and Rural Jobs Act (GARGJA) provides capital for small businesses in rural Georgia. The Georgia Department of Community Affairs (DCA) certified $100 million in capital investment authority to rural funds. The investment capital must be deployed to small businesses that are in agricultural, manufacturing, health care, technology or transportation sectors. The rural funds raise capital from investors in exchange for tax credits. The state tax credit is capped at $15 million annually for 2019 through 2022 ($60 million total). The investment funds must document job creation and retention, average compensation, and rural impact. The funds must demonstrate that investments will generate more state revenue than they receive in tax credits.

Researchers utilized the IMPLAN model to determine the economic and fiscal impact of the GARJA Program. The analysis used actual data provided by the firms (funds) that received investment allocations from the state. The report found that $99.8 million was invested in 33 rural companies and assumed that investment was directly responsible for the creation or retention of 1,000 jobs, which generated nearly $50 million in personal income. The created/retained jobs (direct) and related activity (indirect and induced) were projected to generate $23.4 million in revenue annually (includes state and local), with roughly $10.7 million accruing to the state. Based on these assumptions and findings, the gross return on investment was 1.56 after 10 years. Put another way, the state could expect to recoup the cost of the credits and an additional 56% in return, provided the new/retained jobs were maintained for 10 years. The analysis did not consider any alternative use of state funds (i.e., the benefits if tax credit monies had been used for a different purpose).

Maine New Markets Capital Investment Program (2017)[17]

Maine enacted the New Markets Capital Investment Program (NMTC) in 2011, modeled after the federal NMTC Program but with a refundable tax credit. As of 2016, 10 firms in eight economically distressed communities received $183 million in qualified low-income community investments and four businesses were able to attract an additional $130 million in investments as a result of the NMTC. The analysis found that the NMTC resulted in the creation or retention of 764 direct jobs, an estimated 1,034 indirect jobs and 781 temporary positions. The analysis determined that investors had received $76 million in tax credits and $16 million in retained investments/fees to offset the $183 million in qualified investments. The projected net state budget impact was $16 million for the period 2013 to 2021. Community development entities asserted that it was likely that investments would not have occurred in the absence of the tax credit, as investors would have sought out tax credit investment opportunities in other states.

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[16] "Fiscal Impact of the Georgia Rural Jobs Tax Credit," Georgia Tech Center for Economic Development Research (June 2020).

[17] "New Markets Capital Investment Program," Office of Program Evaluation and Government Accountability of the Maine State Legislature (March 2017).

Economic Evaluation for Select State Economic Development Incentive Programs (2017)[18]

Florida's Capital Investment Tax Credit (CITC) was established in 1998 and was created to incentivize designated high-impact sectors to build or expand in the state.[19] Program participants must create or maintain a minimum of 100 new jobs in Florida and incur $25 million in construction costs (new or expansion). Qualifying businesses can take credits annually for a 20-year period following the operation start date of the new or expanded facility. The CITC Program offers three tiers of tax incentives based on eligible capital costs of the project: $25 million in capital costs (50% credit), $50 million (75% credit) and $100 million (100% credit). Since the start of the program, 43 projects have applied and received approval.

For this report, the Office of Economic and Demographic Research (EDR) and the Office of Program Policy Analysis and Government Accountability (OPPAGA) evaluated the CITC Program from FY 2012-13 through FY 2014-15. A total of nine projects were evaluated during this three-year period. Project recipients were mainly from the manufacturing (33.3%) and the professional, scientific, and technical services sectors (33.3%). Eight projects received other incentives in addition to the CITC funding. Over the reporting window, a total of $66.7 million in tax credits were claimed and $70.2 million in capital investments were reported as a result of the CITC. Approximately 542 jobs were created with an average annual wage of $87,956. State tax revenues increased $28.9 million over the three-year window, resulting in an ROI of 0.43 (i.e., 43% of the credit cost was offset) for the nine projects. The analysis noted various factors that could impact the ROI for CITC projects. First, most projects (eight of the nine) received bundled incentive packages therefore a portion of the capital investment could be attributable to other incentives. Second, the timing of the capital investment impacts the ROI if it occurred before or during the three-year analysis window. Lastly, the analysis found that the ROI was impacted by the level of credit claimed; the more credit claimed, the lower the ROI.

12th Annual Report to the Governor Andrew M. Cuomo and the Legislature on the New York State Certified Capital Company Program (2011)[20]

New York's Certified Capital Law was designed to encourage investment in the state's venture capital markets to promote the creation of new jobs and spur economic growth. The program provided $400 million in dollar-for-dollar tax credit incentives for insurance companies that invest in certified capital companies (CAPCOs) from inception of the program to December 31, 2010. CAPCOs invested in 184 qualified businesses, in amounts ranging from $25,000 to $6.2 million for an individual entity. Of the 184 firms, 98 had less than $1 million in assets at the time of initial investment. After $324.6 million was invested in the program, New York realized a net increase of 188 jobs, with 62 businesses reducing employees, and only 9 entities reported employee growth of more than 50. Employee data was not available for 61 businesses.

Certified Capital Companies Program (2009)[21]

Washington D.C.'s Certified Capital Companies (CAPCO) Act of 2003 was intended to stimulate local business development through job creation within the District of Columbia. The district's program cost $76 million, including $54 million in set-up costs and $22 million in investments into 15 businesses from 2005

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[18] "Economic Evaluation for Select State Economic Development Incentive Programs," Office of Economic and Demographic Research (January 2017).
[19] The CITC is not the same program reflected in Table 3.1.
[20] "12th Annual Report to the Governor Andrew M. Cuomo and the Legislature on the New York State Certified Capital Company Program," New York State Insurance Department (June 2011).
[21] "Certified Capital Companies Program," Office of the District Columbia Auditor (March 2009).

to 2009, during which time, 31 new jobs were created. The Auditor concluded the CAPCO Program failed to achieve the desired impact due to poor government management of an inefficient and expensive program.

Tax Credit Plan

Act 48 of 2017 directs the IFO to review tax credits and develop a tax credit plan for all tax credits subject to review. The act states that tax credit plans should include performance metrics for each credit. The act does not specify any other elements of the tax credit plan. For this review, the IFO defined the tax credit plan more broadly to include the following elements: (1) the general findings of the review, (2) specific recommendations, including performance metrics and (3) key decision points for policymakers to consider.

General Findings

For this report, the IFO identified similar programs in other states, reviewed the research available and spoke with stakeholders, as well as the agencies that administer the tax credit.

The following bullet points summarize the main findings of this research:

- The first rural growth funds were approved in 2021, when DCED approved four funds with total investment authority of $50 million ($12.5 million each), $30 million of which ($7.5 million each) represented credit-eligible capital contributions.
- The funds have up to three years from the closing date to invest capital in approved rural businesses. According to the latest data available, three rural growth funds provided $7.3 million in capital to four rural businesses located in Adams, Berks, Luzerne and Mercer counties. Based on filled reports, 106 jobs have been created or retained due to the program.
- Because the RJITC is still in the early stages of the program, the IFO does not have sufficient data to compute an economic impact or return on investment (ROI).
- Evaluations of similar programs in other states find concerns regarding program effectiveness and efficiency.
- Rural growth funds have an incentive to make investments that provide the highest economic return to their investors instead of those that provide the greatest benefit to state residents.
- The credit provides significant benefits for the fund, even if they must repay some portion of the tax credits upon exit from the program. For example, the funds raised $50 million to invest in rural businesses (typically loans) for seven years. The investors receive $30 million in tax credits to subsidize the investment, repayment of the $50 million in loans (or equivalent equity), plus any applicable interest and fees.

Specific Recommendations

Based on the general findings, the IFO submits the following recommendations to enhance the efficiency of the tax credit and improve its ability to achieve its goals and purpose.

The program would be more effective as a loan program administered by DCED.

Under the current program, rural growth funds invest to maximize return and retain state funds upon exiting the program after seven years. DCED could invest funds strategically to maximize the benefit to the Commonwealth. As the initial loans are repaid, DCED could loan the returned funds to additional rural businesses. In this way, the initial state investment continues to provide benefits to rural businesses.

Additional funding should not be allocated until the impact of the initial $30 million in tax credits can be fully assessed.

Studies of similar programs in other states note concerns with program effectiveness and efficiency. Pennsylvania should thoroughly evaluate the impact of the existing program before additional funds are appropriated, particularly because this program provides significant benefits to rural growth funds and it is unclear how much of that benefit remains in the state.

Key Decision Points

In addition to the specific recommendations above, policymakers should also consider general issues that merit discussion related to the RJITC. These issues are strategic and will be related to the overall goals and purpose of the tax credit as envisioned by policymakers.

- Does the program deliver sufficient economic benefits to warrant additional funds in the future?
- If future funding is justified, should the funds be allocated to DCED for implementation of a rural business loan program in lieu of the current program?
- If the current program is retained, does the program provide greater benefits to the rural businesses it is meant to serve or to private investment firms?
- Should rural growth funds be permitted to retain the credit-eligible contribution amounts? Should this portion be deposited back into a fund and redistributed, with the fund keeping only a management fee?
- Is the current repayment penalty ($30,000 per job created or retained) effective? How does a firm demonstrate that a job is retained? Should only newly created jobs be used to compute penalties?
- What level of compensation do the investment firms receive in administrative costs or management fees? Those data won't be available until the rural growth funds exit the program.

Conclusion

Act 48 requires that the IFO make a determination regarding whether the tax credit has achieved its goals and purpose. For this review, the analysis establishes the specific and quantifiable program goals as:

- Stimulate business development in rural areas.
- Retain and attract new rural businesses and industry to the Commonwealth.
- Create family-sustaining rural jobs.

The analysis establishes the program purpose as:

- Stimulate economic growth and job creation in rural areas by providing rural business owners, who may otherwise have difficulty obtaining investments, with increased access to capital for business development.

As noted, this program is relatively new and less than one year of data was available for review. Therefore, the analysis defers comment regarding whether the tax credit has achieved its assumed goals and purpose. Additional data are needed to make that determination.

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Appendix

Performance-Based Budgeting and Tax Credit Review Schedule

Year	Performance-Based Budgets					
1	Corrections	Board of Probation and Parole	PA Commission on Crime & Delinquency	Juvenile Court Judges' Commission	Banking and Securities	General Services
2	Economic & Community Development	Human Services – Part 1	Health	Environmental Protection	PA Emergency Management Agency	State
3	PennDOT	Human Services – Part 2	State Police	Military & Veterans Affairs		
4	Education	Human Services – Part 3	Aging	PA Historical & Museum Commission	Agriculture	Labor and Industry
5	Drug and Alcohol Programs	Insurance	Revenue	Executive Offices	Conservation and Natural Resources	
Year	**Tax Credits**					
1	Film Production	New Jobs	Historic Preservation Incentive			
2	Research and Development	Keystone Innovation Zones	Mobile Telecom and Broadband	Organ and Bone Marrow		
3	Neighborhood Assistance	Resource Enhancement and Protection (REAP)	Entertainment Economic Enhancement Program	Video Game Production	Keystone Special Development Zones	
4	Educational Tax Credits	Coal Refuse and Reclamation	Mixed-Use Development	Brewers'		
5	Resource Manufacturing	Manufacturing and Investment	Waterfront Development	Rural Jobs and Investment		

IFO Independent Fiscal Office

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