DEPARTMENT OF TAXATION
2012 Fiscal Impact Statement

1. **Patron** Ronald A. Villanueva

2. **Bill Number** HB 335
   House of Origin:
   X **Introduced**
   _____ **Substitute**
   _____ **Engrossed**

   Second House:
   _____ **In Committee**
   _____ **Substitute**
   _____ **Enrolled**

3. **Committee** House Finance

4. **Title** Income Tax: Subtraction for Investment in Small Businesses

5. **Summary/Purpose:**

This bill would allow an individual and corporate income tax subtraction for any income taxed as (i) a gain for federal income tax purposes attributable to an investment in a small business and held by the individual for at least five years or (ii) investment services partnership interest income (otherwise known as investment partnership carried interest income) for federal income tax purposes that is attributable to an investment in a small business. The amount of the subtraction would be limited to gain attributable to the first $500,000 that is invested, regardless of the taxable year or years in which the investment was made.

Under this bill, a taxpayer would not be allowed to claim this subtraction and another Virginia deduction or subtraction for the same gain or investment services partnership interest income. In addition, individuals and estates and trusts would not be able to claim this subtraction and the Qualified Equity and Subordinated Debt Investment Tax Credit.

This bill would be effective for investments made on and after January 1, 2012.

6. **Budget amendment necessary:** Yes.
   Page 1, Revenue Estimate

7. **Fiscal Impact Estimates are:** Preliminary. (See Line 8.)

8. **Fiscal implications:**

<u>Administrative Costs</u>

The Department considers implementation of this bill as routine, and is not requesting additional funding.

<u>Revenue Impact</u>

This bill would have an unknown negative impact on General Fund revenue. The Department is unable to determine whether taxpayers would prefer this subtraction over other Virginia subtractions or deductions or the qualified equity and subordinated debt investment tax credit.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Qualified Equity and Subordinated Debt Credit

Under current law an individual or corporation is allowed a tax credit for investments made to a qualified business. The total amount of the tax credits that may be granted to taxpayers is capped at $3 million. The $3 million is bifurcated, with one-half of the $3 million reserved for qualified businesses created to commercialize research developed at or in partnership with an institution of higher education and the remaining portion available for all other qualified businesses.

A "qualified business" is one that has annual gross revenues of no more than $3 million in its most recent fiscal year; has its principal office or facility in the Commonwealth; is engaged in business primarily in or does substantially all of its production in the Commonwealth; and has not obtained during its existence more than $3 million in aggregate gross cash proceeds from the issuance of its equity or debt investments except for those from banking or savings and loan institutions.

Qualified businesses include those related to advanced computing, advanced materials, advanced manufacturing, agricultural technologies, biotechnology, electronic device technology, energy, environmental technology, medical device technology, nanotechnology, or any similar technology-related field.

No investment qualifies for this credit if the otherwise qualified business performs research in Virginia on human cells or tissue derived from induced abortions or from stem cells obtained from human embryos. This restriction does not apply to qualified businesses that conduct research using stem cells other than embryonic stem cells.

Capital Gain Subtraction

Current law allows an individual and corporate income tax subtraction for income taxed for federal income tax purposes as a long-term capital gain or as investment services partnership interest income (otherwise known as investment partnership carried interest income). The gain must be related to investments in "qualified businesses" as defined for the purposes of the Qualified Equity and Subordinated Debt Credit (QESDC), or in any other technology business approved by the Secretary of Technology, provided its principal office or facility is in the Commonwealth and it has less than $3 million in annual revenues in the fiscal year prior to the investment. A taxpayer who claims a tax credit for investment in a qualified business under the QESDC would not be allowed to claim this subtraction relating to investments in the same business.

To qualify for the subtraction, the related investment must currently be made between April 1, 2010 and June 30, 2013.

Proposal

This bill would allow an individual and corporate income tax subtraction for any income taxed as (i) a gain for federal income tax purposes attributable to an investment in a small business and held by the individual for at least five years or (ii) investment services partnership interest income (otherwise known as investment partnership carried interest income) for federal income tax purposes that is attributable to an investment in a small business. The amount of the subtraction would be limited to gain attributable to the first $500,000 that is invested, regardless of the taxable year or years in which the investment was made.

For purposes of this subdivision, a "small business" would mean a business that (a) has its principal office or facility in the Commonwealth and (b) immediately after such investment and at all times prior to such investment, had aggregate assets that totaled less than $50 million in cash plus the aggregate adjusted bases of all other property held by the business.

Under this bill, a taxpayer would not be allowed to claim this subtraction and another Virginia deduction or subtraction for the same gain or investment services partnership interest income. In addition, individuals and estates and trusts would not be able to claim this subtraction and the Qualified Equity and Subordinated Debt Investment Tax Credit.

This bill would be effective for investments made on and after January 1, 2012.

Similar Bills

Executive bills:

House Bill 585 and Senate Bill 344 would allow an individual income tax credit for certain investments made to small businesses.

House Bill 714 and **Senate Bill 368** would extend the time during which the major business facility job tax credit may be taken over a two-year period through 2014.

House Bill 1013 and **Senate Bill 226** would extend the subtraction from individual and corporate income tax for capital gains to apply to investments in qualified businesses made through June 30, 2015.

Other bills:

House Bill 111 would grant an individual or corporate income tax credit, equal to $1,000, for each new full-time job, up to 50, that a small business creates in Virginia.

House Bill 149 and **Senate Bill 61** would reduce the corporate income tax rate to 3% for 3 years for corporations that locate satellite offices in certain localities.

House Bill 191 would allow a corporate or individual income tax credit, equal to $2,500, to a small business for each new job it creates in Virginia and fills with a graduate of a Virginia college or university.

House Bill 228 would create a corporate income tax credit for certain large federal government contractors equal to five percent of the value of new qualified subcontracts or the increase in the existing subcontracts with small businesses located in HUB zones or Enterprise Zones or are minority-owned, women-owned, or veteran-owned business.

House Bill 783 and Senate Bill 262 would allow a tax credit to individuals and to estates and trusts for the investment into a microenterprise located in a HUBZone, a green microenterprise or any other type of microenterprise. The credit would be equal to 25 percent of an investment into a microenterprise located in a HUBZone, 25 percent of an investment into a green microenterprise or 20 percent of an investment into any other type of microenterprise, phased-in over three taxable years.

cc : Secretary of Finance

Date: 1/28/2012 tlg
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