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SENATE BILL NO. 110

AMENDMENT IN THE NATURE OF A SUBSTITUTE

(Proposed by the Senate Committee on Finance and Appropriations
on January 29, 2020)

(Patron Prior to Substitute—Senator Howell)

A BILL to amend and reenact §§ 58.1-439.12:08 and 58.1-439.12:11 of the Code of Virginia, relating to research and development tax credits; sunset; aggregate caps.

Be it enacted by the General Assembly of Virginia:

1. That §§ 58.1-439.12:08 and 58.1-439.12:11 of the Code of Virginia are amended and reenacted as follows:

§ 58.1-439.12:08. Research and development expenses tax credit.

A. As used in this section, unless the context requires a different meaning:

"Virginia base amount" means the base amount as defined in § 41(c) of the Internal Revenue Code, as amended, that is attributable to Virginia, determined by (i) substituting "Virginia qualified research and development expense" for "qualified research expense"; (ii) substituting "Virginia qualified research" for "qualified research"; and (iii) instead of "fixed base percentage," using:

1. The percentage that the Virginia qualified research and development expense for the three taxable years immediately preceding the current taxable year in which the expense is incurred is of the taxpayer's total gross receipts for such years; or

2. The percentage that the Virginia qualified research and development expense for the applicable number of taxable years immediately preceding the current taxable year in which the expense is incurred is of the taxpayer's total gross receipts for such years, for the taxpayer that has fewer than three but at least one prior taxable year.

"Virginia gross receipts" means the same as "gross receipts" as defined in § 58.1-3700.1.

"Virginia qualified research" means qualified research, as defined in § 41(d) of the Internal Revenue Code, as amended, that is conducted in the Commonwealth.

"Virginia qualified research and development expenses" means qualified research expenses, as defined in § 41(b) of the Internal Revenue Code, as amended, incurred for Virginia qualified research.

B. For taxable years beginning on or after January 1, 2011, but before January 1, 2022 2030, a taxpayer shall be allowed a credit against the tax levied pursuant to § 58.1-320 or 58.1-400 in an amount equal to (i) 15 percent of the first \$300,000 in Virginia qualified research and development expenses paid or incurred by the taxpayer during the taxable year or (ii) 20 percent of the first \$300,000 in Virginia qualified research and development expenses paid or incurred by the taxpayer during the taxable year if the Virginia qualified research was conducted in conjunction with a public or private institution of higher education in the Commonwealth, to the extent the expenses exceed the Virginia base amount for the taxpayer.

C. 1. Effective for taxable years beginning on or after January 1, 2016, at the election of the taxpayer, the credit otherwise allowed under this section shall be computed under this subsection and shall equal 10 percent of the difference of (i) the Virginia qualified research and development expenses paid or incurred by the taxpayer during the taxable year and (ii) 50 percent of the average Virginia qualified research and development expenses paid or incurred by the taxpayer for the three taxable years immediately preceding the taxable year for which the credit is being determined. If the taxpayer did not pay or incur Virginia qualified research and development expenses in any one of the three taxable years immediately preceding the taxable year for which the credit is being determined, the tax credit shall equal five percent of the Virginia qualified research and development expenses paid or incurred by the taxpayer during the relevant taxable year.

2. The aggregate amount of credits allowed to each taxpayer under this subsection shall not exceed \$45,000 for the taxable year, except that the aggregate amount of credits allowed to each taxpayer shall not exceed \$60,000 for the taxable year if the Virginia qualified research was conducted in conjunction with a public institution of higher education in the Commonwealth or a private institution of higher education in the Commonwealth.

D. The aggregate amount of credits available under this section for each fiscal year of the Commonwealth shall be as follows:

1. For taxable years beginning on ~~or~~ and after January 1, 2014, but ~~prior to~~ before January 1, 2016, the total amount of credits granted for each of fiscal years 2015 and 2016 shall not exceed \$6 million.

2. For taxable years beginning on ~~or~~ and after January 1, 2016, but before January 1, 2021, the total amount of credits granted for each fiscal year of the Commonwealth beginning with fiscal year 2017 shall not exceed \$7 million.

3. For taxable years beginning on and after January 1, 2021, the total amount of credits granted for

60 *each fiscal year of the Commonwealth beginning with fiscal year 2022 shall not exceed \$8.4 million.*

61 E. A taxpayer meeting the requirements of this section shall be eligible to receive a tax credit as
62 provided herein. The Department shall develop and publish guidelines for applications and such
63 guidelines shall be exempt from the Administrative Process Act (§ 2.2-4000 et seq.). Applications must
64 be received by the Department no later than ~~July 1~~ *September 1* of the calendar year following the close
65 of the taxable year in which the expenses were paid or incurred. In the event *that* approved applications
66 for the tax credits allowed under this section exceed the amount of credits specified in subsection D for
67 the taxable year, the Department shall apportion the credits by dividing the amount of credits specified
68 in subsection D by the total amount of tax credits approved, to determine the percentage of allowed tax
69 credits each taxpayer shall receive. In the event that the total amount of approved tax credits under this
70 section for all applications for any taxable year is less than the maximum amount of credits for the year
71 as specified in subsection D, the Department shall allocate credits up to the maximum amount as
72 specified in subsection D, on a pro rata basis, to taxpayers who are already approved for the tax credit
73 for the taxable year, in the following amounts:

74 1. If the taxpayer computed the credit pursuant to subsection B, in an amount equal to 15 percent of
75 the second \$300,000 in qualified research expenses during the taxable year or 20 percent of the second
76 \$300,000 in qualified research expenses if the Virginia qualified research was conducted in conjunction
77 with a public institution of higher education in the Commonwealth or a private institution of higher
78 education in the Commonwealth; or

79 2. If the taxpayer computed the credit under subdivision C 1, in an amount equal to the excess of the
80 limitation set forth in subdivision C 2, up to an additional \$45,000 per taxpayer, or \$60,000 per taxpayer
81 if the Virginia qualified research was conducted in conjunction with a public institution of higher
82 education in the Commonwealth or a private institution of higher education in the Commonwealth.

83 F. If the amount of the credit allowed exceeds the taxpayer's tax liability for the taxable year, the
84 amount that exceeds the tax liability shall be refunded to the taxpayer, subject to the limitations set forth
85 in the guidelines developed by the Department.

86 G. Any taxpayer who claims the tax credit for Virginia qualified research and development expenses
87 pursuant to this section shall not use such expenses as the basis for claiming any other credit provided
88 under the Code of Virginia.

89 H. Effective for taxable years beginning on or after January 1, 2016, no taxpayer with Virginia
90 qualified research and development expenses in excess of \$5 million for the taxable year shall claim
91 both the credit allowed pursuant to this section and the credit allowed under § 58.1-439.12:11 for such
92 year.

93 I. Credits granted to a partnership, limited liability company, or electing small business corporation
94 (S corporation) shall be allocated to the individual partners, members, or shareholders, respectively, in
95 proportion to their ownership interests in such entities or in accordance with a written agreement entered
96 into by such individual partners, members, or shareholders, unless the partnership, limited liability
97 company, or electing small business corporation (S corporation) elects for such credits not to be so
98 allocated but to be received and claimed at the entity level by the partnership, limited liability company,
99 or electing small business corporation (S corporation) pursuant to guidelines that shall be issued by the
100 Department for purposes of such election.

101 J. The Department shall adopt guidelines to prescribe standards for determining when research and
102 development is considered conducted in the Commonwealth for purposes of allowing the credit under
103 this section. In adopting guidelines, the Department may consider (i) the location where the research and
104 development is performed; (ii) the residence or business location of the taxpayer or taxpayers conducting
105 the research and development; (iii) the location where supplies used in the research and development are
106 consumed; and (iv) any other factors that the Department deems to be relevant.

107 K. The Tax Commissioner's annual report to the Governor on revenue collections by tax source shall
108 include (i) the total number of applicants approved for tax credits pursuant to this section for the
109 applicable tax year and (ii) the total amount of such tax credits approved for the applicable tax year.

110 L. The Department shall require taxpayers applying for the credit to provide information including (i)
111 the number of full-time employees employed by the taxpayer in the Commonwealth during the taxable
112 year for which the credit is sought; (ii) the taxpayer's sector or sectors according to the 2012 edition of
113 the North American Industry Classification System (NAICS) as published by the United States Census
114 Bureau; (iii) a brief description of the area, discipline, or field of Virginia qualified research performed
115 by the taxpayer; (iv) the total gross receipts or anticipated total gross receipts of the taxpayer for the
116 taxable year for which the credit is sought; and (v) whether the Virginia qualified research was
117 conducted in conjunction with a Virginia public or private college or university. The Department shall
118 aggregate and summarize the information collected and make it available to the Governor and any
119 member of the General Assembly upon request, regardless of the number of taxpayers applying for the
120 credit.

121 M. No tax credit shall be allowed pursuant to this section if the otherwise qualified research and

development expenses are paid for or incurred by a taxpayer for research conducted in the Commonwealth on human cells or tissue derived from induced abortions or from stem cells obtained from human embryos. The foregoing provision shall not apply to research conducted using stem cells other than embryonic stem cells.

§ 58.1-439.12:11. Major research and development expenses tax credit.

A. As used in this section, unless the context requires a different meaning:

"Virginia qualified research" means qualified research, as defined in § 41(d) of the Internal Revenue Code, as amended, that is conducted in the Commonwealth.

"Virginia qualified research and development expenses" means qualified research expenses, as defined in § 41(b) of the Internal Revenue Code, as amended, incurred for Virginia qualified research.

B. For taxable years beginning on or after January 1, 2016, but before January 1, 2022 2030, a taxpayer with Virginia qualified research and development expenses for the taxable year in excess of \$5 million shall be allowed a credit against the tax levied pursuant to § 58.1-320 or 58.1-400 in an amount equal to 10 percent of the difference between (i) the Virginia qualified research and development expenses paid or incurred by the taxpayer during the taxable year and (ii) 50 percent of the average Virginia qualified research and development expenses paid or incurred by the taxpayer for the three taxable years immediately preceding the taxable year for which the credit is being determined. If the taxpayer did not pay or incur Virginia qualified research and development expenses in any one of the three taxable years immediately preceding the taxable year for which the credit is being determined, the tax credit shall equal five percent of the Virginia qualified research and development expenses paid or incurred by the taxpayer during the relevant taxable year.

C. ~~The~~ 1. For taxable years beginning before January 1, 2021, the aggregate amount of credits granted for each fiscal year of the Commonwealth pursuant to this section shall not exceed \$20 million.

2. For taxable years beginning on and after January 1, 2021, the aggregate amount of credits granted for each fiscal year of the Commonwealth pursuant to this section shall not exceed \$24 million.

D. In the event that approved applications for the tax credits allowed under this section exceed \$20 million the limit described in subsection C for any taxable year, the Department shall apportion the credits by dividing \$20 million such limit by the total amount of tax credits approved, to determine the percentage of allowed tax credits each taxpayer shall receive.

E. The amount of the credit claimed for the taxable year shall not exceed 75 percent of the total amount of tax imposed by this chapter upon the taxpayer for the taxable year. Any credit not usable for the taxable year for which the credit was first allowed may be carried over for credit against the income taxes of the taxpayer in the next 10 succeeding taxable years or until the total amount of the tax credit has been taken, whichever is sooner.

F. Any taxpayer who claims the tax credit for Virginia qualified research and development expenses pursuant to this section shall not use such expenses as the basis for claiming any other credit provided under the Code of Virginia.

G. Credits granted to a partnership, limited liability company, or electing small business corporation (S corporation) shall be allocated to the individual partners, members, or shareholders, respectively, in proportion to their ownership interests in such entities or in accordance with a written agreement entered into by such individual partners, members, or shareholders.

H. The Department shall develop and publish guidelines under this section including guidelines for applying for the tax credit. Such guidelines shall be exempt from the Administrative Process Act (§ 2.2-4000 et seq.). Applications for the tax credit must be received by the Department no later than July 1 September 1 of the calendar year following the close of the taxable year in which the expenses were paid or incurred.

The Department shall also adopt guidelines to prescribe standards for determining when research and development is considered conducted in the Commonwealth for purposes of allowing the credit under this section. In adopting guidelines, the Department may consider (i) the location where the research and development is performed; (ii) the residence or business location of the taxpayer or taxpayers conducting the research and development; (iii) the location where supplies used in the research and development are consumed; and (iv) any other factors that the Department deems to be relevant.

I. No tax credit shall be allowed pursuant to this section, if the otherwise qualified research and development expenses are paid for or incurred by a taxpayer for research conducted in the Commonwealth on human cells or tissue derived from induced abortions or from stem cells obtained from human embryos. The foregoing provision shall not apply to research conducted using stem cells other than embryonic stem cells.