DEPARTMENT OF TAXATION
2001 Fiscal Impact Statement

1. Patron Quayle

2. Bill Number SB 1260

House of Origin:
X Introduced
_____ Substitute
_____ Engrossed

Second House:
_____ In Committee
_____ Substitute
_____ Enrolled

3. Committee Senate Finance

4. Title Income Tax Credit: Virginia Technology and Biotechnology Investment Act

5. Summary/Purpose:

This bill would create a number of tax incentives aimed at encouraging the establishment and expansion of small technology and biotechnology corporations. These incentives are:

- A tax credit equal to 15% of the qualified research and development expenditures by technology and biotechnology corporations.
- A tax credit equal to 15% of a qualified investment in a technology or biotechnology corporation.
- The creation of a "Corporation Tax Benefit Certificate Program" which would allow technology and biotechnology corporations to transfer unused but otherwise allowable research and development tax credits or net operating loss ("NOL") carryovers to another corporation taxpayer for a minimum of 75 cents on the dollar.
- Total credits that could be authorized under this bill could not exceed $10 million annually.

This bill is effective for taxable years beginning on or after January 1, 2001.

6. Fiscal Impact Estimates are: Not available. (See line 8.)

6a. Expenditure Impact:

Fiscal Year	*Dollars*	*Positions*	*Fund*
2000-01	$0	0	GF
2001-02 *	$72,998	1	GF
2002-03 *	$58,316	1	GF

*** Does not include systems costs. (See line 8.)**

7. Budget amendment necessary: Yes.
Item(s): 279 and 281, Department of Taxation

8. Fiscal implications:

Administrative Cost

While this bill does have costs associated with systems development, these cannot be ascertained at this time. The cost for implementing a **single** piece of legislation cannot be calculated precisely due to economies of scale. The actual cost to implement **all** legislation enacted during a given session will more than likely be less than the sum of the costs attributed to individual bills. Further, the ability to accurately predict costs is complicated because the department is replacing its current database system. As a result, legislative changes may need to be made to both the current and the future system, depending on the effective date. Therefore, the department is not providing specific systems costs for this bill, but will calculate the total for all tax bills once they have been acted upon favorably in both houses and prior to the conference committee report. The department would incur administrative costs of $72,998 for Fiscal Year 2002 for form revisions, and three additional full-time positions. Continuing costs would be $58,316 for Fiscal Year 2003 and thereafter.

Revenue Estimate

The General Fund revenue impact of this bill is unknown. While each of the proposed credits is capped at $5 million, technology and biotechnology companies and investors in such businesses would be able carry forward unused credits and corporations could purchase unused credits and NOLs from technology and biotechnology corporations. As such, the negative revenue impact of this bill could exceed $10 million in a given fiscal year.

9. Specific agency or political subdivisions affected:

Innovative Technology Authority
Department of Taxation

10. Technical amendment necessary: Yes.

In order to prevent a taxpayer from getting a double benefit from the investment tax credit in this bill and other enacted and proposed investment tax credits, the following technical amendment is suggested:

Page 4, Line 167, At the end of the line
Insert: F. A taxpayer who claims the credit pursuant to this section may not use such qualified investment as the basis for claiming any other credit or grant provided under the Code of Virginia.

11. Other comments:

Generally

The Virginia Technology and Biotechnology Investment Act would create a program of tax credits and benefits for technology and biotechnology companies.

A “Technology Company” would be a corporation having less than 100 employees (75% of whom work in Virginia) that performs research and development for specific commercial or public purposes, conducts pilot scale manufacturing, and/or provides services or products necessary for such research, development and production in Virginia.

A “Biotechnology Company” would be a corporation having less than 100 employees (75% of whom work in Virginia) that performs research and development for medical, pharmaceutical, nutritional, agricultural, or environmental purposes; conducts pilot scale manufacturing; and/or provides services or products necessary for such research, development and production in Virginia.

Biotechnology Research and Development Tax Credit

This bill would create a credit against the corporate income tax for 15% of the qualified research expenditures by technology and biotechnology companies. In general, expenditures that qualify for this credit would be the same as those that qualify for the federal research credit.

The Biotechnology Research and Development Tax Credit (“BRDTC”) would be limited to 50% of the tax liability after being reduced by any other tax credit to which the corporation is entitled or $500,000. In other words, a technology or biotechnology company would reduce its income tax liability by any other corporate income tax credit it had earned. This reduced amount would be multiplied by 50% to determine if the limitation for the BRDTC for the taxable year would be less than $500,000. Unused credits can be carried forward for up to 10 years.

The federal credit is based on (1) excess of the qualified research expenses and (2) basic research payments. Qualified research expenses include wages and salaries paid to individuals engaged in research; supplies, tools and equipment used to conduct research and 65% of fees paid to a research contractor. Basic research payments are amounts paid to educational institutions and nonprofit research organizations to conduct research pursuant to a written agreement.

Technology and biotechnology companies would not be able to claim the BRDTC for otherwise qualifying research expenditures paid out of funds received from an investor claiming the Technology and Biotechnology Investment Tax Credit (see below).

Technology and biotechnology corporations would be prohibited from using expenditures for claiming both the BRDTC and any other credit against the Virginia corporate income tax.

The BRDTC would only be available to corporations subject to the corporate income tax. Technological and biotechnological research companies that are S corporations, limited liability companies, partnerships, or sole proprietorships and pass income through to their owners would not qualify for this credit.

The BRDTC would be limited to $5 million annually. If credits exceed the $5 million annual cap in a taxable year, the Department of Taxation will be responsible for allocating the credits on a pro rata basis.

Technology and Biotechnology Investment Tax Credit

This bill would also create a tax credit for individual, fiduciary, and corporate taxpayers equal to 15% of a qualified investment in a technology or biotechnology corporation. The maximum credit that could be earned for each qualified investment in any taxable year would be $500,000. Like the BRDTC, this credit would be limited to 50% of the tax liability after the application of other corporate income tax credits or $500,000. Any unused portion of the credit could be carried forward for up to 10 years subject to the $500,000 annual limitation.

For the purposes of the Technology and Biotechnology Investment Tax Credit ("TBITC"), a qualified investment includes traditional investments like stock, warrants, options, partnership interests, and participation in joint ventures. In addition, a taxpayer can qualify for the TBITC by purchasing exclusive or nonexclusive licenses or rights to use technology, marketing rights or any similar items.

The TBITC would be limited to $5 million annually. If credits exceed the $5 million annual cap in a taxable year, the Department of Taxation will be responsible for allocating the credits on a pro rata basis.

Corporation Tax Benefit Certificate Program

The bill would authorize the Innovative Technology Authority ("ITA"), with the assistance of the Department of Taxation, to establish a program to allow technology or biotechnology corporations to sell unused carryovers of the BRDTC and any NOL to other corporations. These purchasing corporations would be able to use the BRDTC and NOLs to reduce their Virginia income tax.

ITA would receive, review and approve applications from technology or biotechnology corporations wishing to sell unused credits and NOL. Corporations wishing to purchase the tax benefits would also apply to the ITA. ITA would facilitate negotiations for the transfer of the tax benefits between the technology and biotechnology corporations and purchasing corporations. No transfer would be made without a written agreement stipulating the sales price of the transfer and any other terms the parties may deem necessary. The minimum sales price of such transfers would be 75% of the value of the tax benefit. In other words, if a technology corporation earned a $100 BRDTC, the minimum another corporation would have to pay for the credit is $75.

Pursuant to the written agreement, ITA would issue a Corporation Tax Benefit Certificate to a purchasing corporation displaying the amount of the tax benefit. Purchasing corporations would have to attach a copy of the certificate to their income tax returns in order to redeem the tax benefit.

Other legislation

House Bill 1989 and **House Bill 2542** would allow technology and biotechnology companies to sell earned but unused income tax credits to corporate taxpayers for at least 75% of face value.

House Bill 2184 would create a tax credit equal to 50% of qualified research and development expenses incurred by technology and biotechnology corporations in Virginia and a tax credit equal to 50% of basic research payments for research and development done in the Commonwealth. Unused credits could be carried over for up to 10 taxable years. Unused research and development tax credits could be sold for at least 75% of face value.

House Bill 2466 would amend the Qualified Equity and Subordinated Debt Investments Tax Credit to (i) increase the total amount of tax credit pool from $5 million to $20 million; (ii) change the $50,000 cap per taxpayer to the amount equal to 10% of the tax credit pool; (iii) reduce the tax credit from 50% to 25% of a qualified investment; and (iv) reduce the equity investment holding period requirement from 5 to 2 years.

House Bill 2467 would create an income tax credit for individuals, partnerships, and corporations that invest in small technology businesses. An individual taxpayer would be allowed a credit equal to 25% of an investment up to $50,000. A partnership or a corporation is allowed a credit equal to 25% of an investment up to $100,000.

Investments/Expenditures Qualifying for Multiple Credits

In 1998, the General Assembly established the Qualified Equity and Subordinated Debt Investments Tax Credit ("QESDITC") for individual and fiduciary income taxpayers that invest in qualified Virginia small business ventures that have annual gross receipts of $5 million or less. It is possible that the technology and biotechnology companies targeted by the TBITC could also qualify for the QESDITC. In order to qualify for the TBITC, the target business must have 100 employees or less. If a technology and biotechnology company has gross receipts of $5 million or less and 100 or less employees, it is possible that an investment made in such a company could meet the qualifications of both credits. This bill would not prohibit individuals, trusts, and estates from claiming both credits for the same investment. A technical amendment has been suggested so that an investment that qualifies for the TBITC would not be able to used as the basis for claiming any other investment tax credit or grant.

In addition, the General Assembly enacted legislation in the 2000 session that established the Tobacco-Dependent Localities Technology investment Tax Credit ("TDLTITC"), and another investment tax credit has been introduced in this session for which investments made in technology or biotechnology businesses under this bill could qualify (see House Bill 2467 above). The TDLTITC contains a provision that would prevent investments from being used for the TDLTITC and any other investment tax credit. House Bill 2467 includes a similar provision.

Along with the TDLTITC, the General Assembly established the Tobacco-Dependent Localities Research and Development Tax Credit ("TDLRDTC"). Expenditures qualifying for the TDLRDTC could also quality for the BRDTC under this bill. In addition, House Bill 2184 proposes two income tax credits based on research and development expenditures. The TDLRDTC includes a provision that would prevent expenditures that quality for the TDLRDTC from being used to claim any other Virginia Tax Credit. This bill also includes such a provision. House Bill 2184 includes a similar a provision for the one of its proposed credits but not the other.

The following tables illustrate the similarities between the qualification requirements for the QESDITC, the TDLTITC, the TDLRDTC, and the proposed investment and research and development tax credits:

	Targeted Business for Investment Credits	**Qualified Business for R & D Expenditures Credits**
QESDITC (HB 2466)	Virginia small businesses that have annual gross receipts of $5 million or less.	
HB 2467	Technology or biotechnology businesses that have 10 or less employees.	
TDLTITC	Technology or biotechnology businesses located in tobacco-dependent localities and meeting criteria established by the Tobacco Indemnification and Community Revitalization Commission.	
HB 2184		Technology or biotechnology businesses that have 100 or less employees.
TDLRDTC		Technology or biotechnology businesses located in tobacco-dependent localities and meeting criteria established by the Tobacco Indemnification and Community Revitalization Commission.
SB 1260	Technology or biotechnology businesses that have 100 or less employees.	Technology or biotechnology businesses that have 100 or less employees.

cc: Secretary of Finance

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