

DEPARTMENT OF TAXATION

2009 Fiscal Impact Statement

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| 1. Patron John M. O'Bannon, III | 2. Bill Number <u>HB 2455</u> |
| 3. Committee House Science and Technology | House of Origin:
<u> X </u> Introduced
<u> </u> Substitute
<u> </u> Engrossed |
| 4. Title Qualified equity and subordinated debt
investments tax credit; qualified businesses | Second House:
<u> </u> In Committee
<u> </u> Substitute
<u> </u> Enrolled |

5. Summary/Purpose:

This bill would modify the Qualified Equity and Subordinated Debt Investment Tax Credit to allow a tax credit for individuals or corporations for investments in businesses related to advanced computing, advanced materials, agricultural technologies, biotechnology, electronic device technology, energy, environmental technology, medical device technology, nanotechnology, or any similar technology-related field. One-half of the \$3 million authorized annually would be reserved for "commercialization investment" that supports research developed at or in partnership with an institution of higher education.

This bill would be effective for taxable years beginning on or after January 1, 2009.

This bill is a recommendation of the Joint Subcommittee studying biosciences and biotechnology.

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

7. Budget amendment necessary: No.

8. Fiscal implications:

Administrative Impact

TAX has not assigned any administrative costs to this bill because the changes required by a single bill such as this can be implemented as part of the annual changes to our systems and forms. As stand-alone legislation, TAX considers implementation of this bill as "routine," and does not require additional funding.

TAX will provide specific administrative costs on any legislation that is not "routine." Additionally, TAX will review all state tax legislation likely to be enacted prior to the passage by each house. If the aggregate number of routine bills likely to pass either house is unusually large, it is possible that additional resources will be required. If so, TAX will identify the costs at that time.

Revenue Impact

The revenue impact of this bill is unknown. Historically, applications for this credit have exceeded the annual cap, so the total amount of credits allocated has been equal to the annual cap. However, the amount of credits actually claimed on tax returns has been significantly less than the annual cap, probably because not all of the taxpayers have sufficient taxable income to fully utilize the credit in the year it is earned.

About half of the existing credit applications have involved businesses that would not qualify for the credit under the proposed definition of a “qualified business,” such as restaurants, hotels, retail establishments and other miscellaneous businesses. Therefore, it is possible that applications for the credit under this bill would not reach the \$3 million cap.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Current Law

Under current law an individual or corporation is allowed a tax credit for investments made to a qualified business. While the statute caps the total amount of credits at \$5 million, budget language has imposed a \$3 million cap since 2006.

Under current law, a “qualified business” 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.

In addition, a qualified business is limited to businesses that are not categorized as the following: banks; savings and loan institutions; credit or finance; financial, broker or investment; businesses organized for the primary purpose of rendering professional services; accounting; government, charitable, religious or trade institutions or organizations; conventional coal, oil and gas, and mineral exploration; insurance; real estate design or engineering; construction or construction contracting; business consulting or business brokering; residential housing, real estate brokerage, sale or leasing businesses, or real estate development; or any other business which the Department of Taxation determines by regulation to be against the public interest or in violation of the law.

Proposal

This bill would modify the definition of a “qualified business” eligible for the Qualified Equity and Subordinated Debt Investment Tax Credit. The bill would limit the credit to individuals or corporations making investments in businesses related to advanced computing, advanced materials, agricultural technologies, biotechnology, electronic device technology, energy, environmental technology, medical device technology, nanotechnology, or any similar technology-related field. The Department of Taxation would be responsible for determining any similar technology-related business which may also qualify.

The proposed definition of a “qualified business” would exclude many types of businesses currently eligible for the credit. For example, TAX received a total of approximately 46 credit applications for 2008. If this bill had been in effect for 2008, 30 of these applicants would not qualify under the proposed definition of “qualified business.” These included restaurants and hotels, beverage manufacturers, warehousing and storage facilities, wood manufacturers, recreational facilities, parking facilities, and various other retail, wholesale and service businesses.

This bill would bifurcate the existing cap of \$3 million for credits earned each year. One-half of the \$3 million would be reserved for qualified businesses created to commercialize research developed at or in partnership with an institution of higher education. Any portion of the \$3 million authorization that was not used for “commercialization investment” would be available for all other qualified businesses. Under existing regulations, if applications for the credit exceed the annual cap the credits are allocated pro rata among all applicants. With the bifurcation of the cap, there could be separate prorations for commercialization investments and all other qualified businesses.

This bill would be effective for taxable years beginning on or after January 1, 2009.

Other Legislation

Senate Bill 1338 is similar to this bill, but it would also modify the Commonwealth Research Commercialization Fund and the duties and responsibilities of the Virginia Economic Development Partnership Authority.

cc : Secretary of Finance

Date: 1/25/2009 TLG
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