

DEPARTMENT OF TAXATION 2021 Fiscal Impact Statement

1. **Patron** Mamie E. Locke

2. **Bill Number** SB 1112

3. **Committee** Senate Finance and Appropriations

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

4. **Title** Research and Development Tax Credits;
Expansion to Bank Franchise Tax

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would permit taxpayers subject to the Bank Franchise Tax to claim the Research and Development Expenses Tax Credit and the Major Research and Development Expenses Tax Credit. Under current law, the credits may be claimed only against the individual and corporate income tax.

This bill would be effective for taxable years beginning on and after January 1, 2021.

6. **Budget amendment necessary:** No.

7. **No Fiscal Impact:** (See Line 8).

8. **Fiscal implications:**

Administrative Costs

The Department of Taxation ("the Department") considers implementation of this bill as routine, and does not require additional funding.

Revenue Impact

This bill would have no impact on General Fund revenues.

Both of these credit programs are currently oversubscribed by a significant amount. For Taxable Year 2019, taxpayers requested \$20.8 million of Research and Development Expenses Tax Credits, in excess of the \$7 million cap. Similarly, taxpayers requested \$125.8 million of Major Research and Development Expenses Tax Credits for Taxable Year 2019, in excess of the \$20 million cap.

This bill would expand both credits to a new tax type, but would not increase the annual credit caps for either program. For purposes of both programs, credit allocations are required to be prorated to the extent approved credit claims exceed the respective annual

credit caps. Therefore, allowing more taxpayers to apply for these credits may result in increased proration and reduce credit allocations on a per taxpayer basis.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: Yes.

The Department understands that the intent of this bill is to permit taxpayers subject to the Bank Franchise Tax to claim the Research and Development Expenses Tax Credit and the Major Research and Development Expenses Tax Credit. This fiscal impact statement was drafted based on that understanding.

However, as drafted, this bill would not do so with respect to the Major Research and Development Expenses Tax Credit. If that is the Patron's intent, the Department suggests the following technical amendment:

Page 3, Line 155
Strike: or
Insert: a comma after 58.1-320

Page 3, Line 155, after 58.1-400
Insert: 58.1-1202

11. Other comments:

Research and Development Expenses Tax Credit

The Research and Development Expenses Tax Credit is a refundable individual and corporate income tax credit for conducting qualified research and development in Virginia. The credit is comprised of a base credit and a supplemental credit that is available only to the extent that the total amount of base credits granted for a fiscal year is less than the annual credit cap. A taxpayer may compute the base credit using the primary method for determining the credit or elect to compute the base credit using the alternative simplified method ("simplified method") for determining the credit.

The base credit for a taxpayer using the primary method is equal to: (i) 15 percent of the Virginia qualified research and development expenses paid or incurred by the taxpayer during the credit year (up to a \$45,000 credit), or (ii) 20 percent of the Virginia qualified research and development expenses paid or incurred by the taxpayer during the credit year if the Virginia qualified research was conducted in conjunction with a Virginia public or private college or university (up to a \$60,000 credit), to the extent such expenses exceed the taxpayer's Virginia base amount.

The base credit for a taxpayer that elects to utilize the simplified method is equal to 10 percent of the difference between:

- The Virginia qualified research and development expenses paid or incurred by the taxpayer during the taxable year; and
- 50 percent of the average Virginia qualified research and development expenses paid or incurred by the taxpayer for the three immediately preceding taxable years.

If a taxpayer did not pay or incur Virginia qualified research and development expenses in any one of the three preceding taxable years, the base credit is equal to 5 percent of the Virginia qualified research and development expenses paid or incurred by the taxpayer during the relevant taxable year. The annual base credit amount allowed may not exceed (i) \$45,000 or (ii) \$60,000 if the Virginia qualified research was conducted in conjunction with a Virginia public or private college or university.

When the credit was first enacted, it was subject to a \$5 million annual cap. The cap was increased to \$6 million for Taxable Years 2014 and 2015, to \$7 million for Taxable Year 2016 through Taxable Year 2020, and to \$7.77 million for Taxable Year 2021 and thereafter. No taxpayer may claim both this credit and the Major Research and Development Expenses Tax Credit for the same taxable year.

Major Research and Development Expenses Tax Credit

Virginia allows a nonrefundable individual and corporate income tax credit for incurring more than \$5 million of Virginia qualified research and development expenses during a taxable year. The amount of the credit is equal to 10 percent of the difference between:

- The Virginia qualified research and development expenses paid or incurred by the taxpayer during the taxable year; and
- 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 years.

If a 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 credit is equal to 5 percent of the Virginia qualified research and development expenses paid or incurred by the taxpayer during the relevant taxable year.

The Major Research and Development Expenses Tax Credit was subject to an annual credit cap of \$20 million for Taxable Year 2016 through Taxable Year 2020. The credit is subject to an annual cap of \$24 million for Taxable Year 2021 and thereafter.

Proposed Legislation

This bill would permit taxpayers subject to the Bank Franchise Tax to claim the Research and Development Expenses Tax Credit and the Major Research and Development Expenses Tax Credit. Under current law, the credits may be claimed only against the individual and corporate income tax.

This bill would be effective for taxable years beginning on and after January 1, 2021.

Similar Legislation

House Bill 1916 is substantively identical to this bill.

cc : Secretary of Finance

Date: 1/18/2021 JLOF
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