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SENATE BILL NO. 1048

Offered January 11, 2023

Prefiled January 8, 2023

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 expenses tax credits.

Patron—McPike

Referred to Committee on Education and Health

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. 1. For taxable years beginning on or after January 1, 2011, but before January 1, 2021, 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.

2. For taxable years beginning on or after January 1, 2021, but before January 1, 2025, a taxpayer shall be allowed a credit against the tax levied pursuant to § 58.1-320, 58.1-400, or 58.1-1202 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

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59 not exceed \$60,000 for the taxable year if the Virginia qualified research was conducted in conjunction
60 with a public institution of higher education in the Commonwealth or a private institution of higher
61 education in the Commonwealth.

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

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

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

69 3. For taxable years beginning on and after January 1, 2021, *but before January 1, 2023*, the total
70 amount of credits granted for each fiscal year of the Commonwealth beginning with fiscal year 2022
71 shall not exceed \$7.77 million.

72 4. *For taxable years beginning on and after January 1, 2023, the total amount of credits granted for*
73 *each fiscal year of the Commonwealth beginning with fiscal year 2024 shall not exceed \$15.77 million.*

74 E. A taxpayer meeting the requirements of this section shall be eligible to receive a tax credit as
75 provided herein. The Department shall develop and publish guidelines for applications and such
76 guidelines shall be exempt from the Administrative Process Act (§ 2.2-4000 et seq.). Applications must
77 be received by the Department no later than September 1 of the calendar year following the close of the
78 taxable year in which the expenses were paid or incurred. In the event that approved applications for the
79 tax credits allowed under this section exceed the amount of credits specified in subsection D for the
80 taxable year, the Department shall apportion the credits by dividing the amount of credits specified in
81 subsection D by the total amount of tax credits approved, to determine the percentage of allowed tax
82 credits each taxpayer shall receive. In the event that the total amount of approved tax credits under this
83 section for all applications for any taxable year is less than the maximum amount of credits for the year
84 as specified in subsection D, the Department shall allocate credits up to the maximum amount as
85 specified in subsection D, on a pro rata basis, to taxpayers who are already approved for the tax credit
86 for the taxable year, in the following amounts:

87 1. If the taxpayer computed the credit pursuant to subsection B, in an amount equal to 15 percent of
88 the second \$300,000 in qualified research expenses during the taxable year or 20 percent of the second
89 \$300,000 in qualified research expenses if the Virginia qualified research was conducted in conjunction
90 with a public institution of higher education in the Commonwealth or a private institution of higher
91 education in the Commonwealth; or

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

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

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

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

106 I. Credits granted to a partnership, limited liability company, or electing small business corporation
107 (S corporation) shall be allocated to the individual partners, members, or shareholders, respectively, in
108 proportion to their ownership interests in such entities or in accordance with a written agreement entered
109 into by such individual partners, members, or shareholders, unless the partnership, limited liability
110 company, or electing small business corporation (S corporation) elects for such credits not to be so
111 allocated but to be received and claimed at the entity level by the partnership, limited liability company,
112 or electing small business corporation (S corporation) pursuant to guidelines that shall be issued by the
113 Department for purposes of such election.

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

120 K. The Tax Commissioner's annual report to the Governor on revenue collections by tax source shall

include (i) the total number of applicants approved for tax credits pursuant to this section for the applicable tax year and (ii) the total amount of such tax credits approved for the applicable tax year.

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

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. 1. For taxable years beginning on or after January 1, 2016, but before January 1, 2021, 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.

2. For taxable years beginning on or after January 1, 2021, but before January 1, ~~2025~~ 2023, 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, 58.1-400, or 58.1-1202 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.

3. *For taxable years beginning on or after January 1, 2023, but before January 1, 2025, 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, 58.1-400, or 58.1-1202 in an amount equal to:*

a. Ten percent, up to the first \$1 million, of the difference between (i) 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.

b. Five percent of the difference in excess of \$1 million between (i) any 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

182 of the three taxable years immediately preceding the taxable year for which the credit is being
183 determined, the tax credit shall equal five percent of the Virginia qualified research and development
184 expenses paid or incurred by the taxpayer during the relevant taxable year.

185 The aggregate amount of credits allowed to each taxpayer under this subdivision 3 shall not exceed
186 \$300,000 for the taxable year, except that the aggregate amount of credits allowed to each taxpayer
187 shall not exceed \$400,000 for the taxable year if the Virginia qualified research was conducted in
188 conjunction with a public institution of higher education in the Commonwealth or a private institution of
189 higher education in the Commonwealth.

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

192 2. For taxable years beginning on and after January 1, 2021, but before January 1, 2023, the
193 aggregate amount of credits granted for each fiscal year of the Commonwealth pursuant to this section
194 shall not exceed \$24 million.

195 3. For taxable years beginning before January 1, 2023, the aggregate amount of credits granted for
196 each fiscal year of the Commonwealth pursuant to this section shall not exceed \$16 million.

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

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

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

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

213 H. The Department shall develop and publish guidelines under this section including guidelines for
214 applying for the tax credit. Such guidelines shall be exempt from the Administrative Process Act
215 (§ 2.2-4000 et seq.). Applications for the tax credit must be received by the Department no later than
216 September 1 of the calendar year following the close of the taxable year in which the expenses were
217 paid or incurred.

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

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