HB 1098

Department of Legislative Services

Maryland General Assembly
2001 Session

FISCAL NOTE

House Bill 1098 (Delegate Barve, *et al.*)
(Montgomery County Administration)

Ways and Means

Maryland Biotechnology Companies - Tax Benefit Certificate Program

This bill creates a Maryland Biotechnology Tax Benefit Certificate Program within the Department of Business and Economic Development (DBED). The purposes of the program are to: (1) encourage the extension of private financial assistance to the biotechnology industry; and (2) allow "new or expanding biotechnology companies" in Maryland with unused research and development tax credits or unused net operating losses to sell those benefits to a corporation.

The bill takes effect July 1, 2001 and sunsets June 30, 2006.

Fiscal Summary

State Effect: General fund revenue decrease of $15 million and Transportation Trust Fund revenue decrease of $5 million in FY 2003 through FY 2006 assuming that the maximum credit certificates are issued each year.

(in dollars)	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006
GF Revenue	$0	($15,000,000)	($15,000,000)	($15,000,000)	($15,000,000)
SF Revenue	0	(5,000,000)	(5,000,000)	(5,000,000)	(5,000,000)
Expenditure	$0	$0	$0	$0	$0
Net Effect	$0	($20,000,000)	($20,000,000)	($20,000,000)	($20,000,000)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Local government revenues would decrease by approximately $1.5 million in FY 2002 through 2006 as a result of corporate taxpayers claiming the credits proposed in the bill.

Small Business Effect: Potential meaningful. To the extent that small businesses are able to either buy or sell net operating losses, these businesses will either realize increased capital or reduced income tax liabilities.

Analysis

Bill Summary: A new or expanding biotechnology company may apply to DBED to transfer tax benefits under the program. A corporation may apply to DBED to receive transferable tax benefits. All applications must be received on or before June 30 for the next succeeding State fiscal year.

DBED is required to evaluate applications for the transfer of tax benefits under the program in a manner that will best stimulate and encourage the extension of private financial assistance to new or expanding biotechnology companies in Maryland.

DBED is required to develop criteria for the approval or disapproval of applications. Approval criteria include: (1) an evaluation of the new or expanding biotechnology company's actual or potential scientific and technological viability; (2) a determination that the new or expanding biotechnology company's principal products or services are sufficiently innovative to provide a competitive advantage; (3) a determination that the new or expanding biotechnology company does not have sufficient resources to operate in the short term or cannot secure financial assistance from venture capital, stock issuance, product sales revenue, a parent corporation or other affiliates, a bank, or any other method of obtaining capital; and (4) a determination that the financial assistance provided under this subtitle demonstrates the prospect of a significant positive change in the new or expanding biotechnology company's net income.

A new or expanding biotechnology company that has had its application approved may surrender the tax benefits that are requested in the application regardless of whether the applicant continues to meet the eligibility criteria in subsequent years. An applicant's transferable tax benefits: (1) are limited to tax benefits that the applicant requests to surrender in its application to DBED; and (2) may not, in total, exceed the maximum amount of tax benefits that the applicant is eligible to surrender.

A new or expanding biotechnology company is not eligible to participate in the program if the company: (1) has demonstrated positive net income in any of the two previous full taxable years of ongoing operations as determined on its financial statements; (2) has demonstrated a ratio in excess of 110% of operating revenues divided by operating expenses in any of the two previous full taxable years of operations as determined on its financial statements; (3) is directly or indirectly at least 50% owned or controlled by another corporation that has demonstrated positive net taxable income in any of the two previous full taxable years of ongoing operations as determined on its financial statements; or (4) is part of a consolidated group of affiliated corporations, as filed for federal income tax purposes, that in the aggregate has demonstrated positive net taxable income in any of the two previous full taxable years of ongoing operations as determined on its combined financial statements.

DBED will issue a business tax benefit certificate to a corporate applicant that is approved to participate in the program. An approved biotech company may sell unused R&D credits and unused net operating losses to a corporation that receives a tax benefit certificate for at least 75% of the value of the unused credit or net operating losses. The amount of the purchased credit or net operating losses is the amount of the credit that may be claimed by the corporation.

DBED may not approve the transfer of more than $20 million of tax benefits for any fiscal year. The maximum lifetime value of tax benefits that a corporation may surrender under the program is $4 million.

A new or expanding biotechnology company that transfers tax benefits under the program may use the private financial assistance received from the corporation that receives the transferred tax benefits to fund operation and development costs including: (1) construction, acquisition, and development of real estate; (2) acquisition of materials; (3) start-up costs; (4) tenant fit-out; (5) working capital; (6) salaries; (7) research and development expenditures; and (8) any other expenses determined by DBED.

A corporation that receives surrendered tax benefits under the program may claim a credit against the State income tax in the amount of the surrendered tax benefits and may apply the credit only in the taxable year in which the credit is acquired. A tax benefit surrendered under the program may be acquired by only one corporation.

Any unused credit that has been surrendered under the Maryland Biotechnology Tax Benefit Certificate Program may not be carried forward to any other taxable years.

DBED and the Comptroller are required to adopt regulations to carry out the provisions of the bill.

Current Law: None applicable.

Background: New Jersey enacted legislation in 1998 that allows biotechnology companies to sell unused R&D credits and net operating losses to other New Jersey corporations. Beginning in fiscal 2002, New Jersey will authorize the transfer of $40 million in tax benefits (for fiscal 2001 it was $50 million).

Connecticut recently enacted legislation that allows small businesses to exchange unused R&D credits for a cash payment from the state in the amount of 65% of the value of the credit.

There are approximately 120 biotechnology companies in Maryland.

State Fiscal Effect: It is not known how many biotechnology companies will have net operating losses or unused R&D credits to sell, the value of these benefits, the number of companies that would purchase net operating losses in order to receive a tax credit certificate, and the tax liabilities of these companies. Because of the bill's July 1, 2001 effective date, it is assumed that tax credits will not be claimed until tax year 2002.

If the maximum $20 million in credit certificates is issued each year, general fund revenues would decrease by $15 million and Transportation Trust Fund (TTF) revenues would decrease by $5 million in fiscal 2003 through 2006 due to the distribution of corporate income tax revenues. Because 75% of all corporate income tax revenues are distributed to the general fund and 25% are distributed to the TTF, credits taken on corporate income tax returns reduce general fund revenues by 75% of the amount of the credits taken and TTF revenues by 25% of the credits taken. In addition, 30% of the 25% of revenue distributed to the TTF is distributed to local governments.

Revenue losses could be offset to some extent should companies selling net operating losses use the cash from the sale to expand. This could lead to increased income tax collections if the company hires more employees and increased property tax revenues due to expanded facilities.

DBED advises that any costs incurred to administer the program would be offset by the processing fees it is authorized to charge applicants for the credit certificate program.

Local Fiscal Effect: Local government revenues would decline as a result of corporate taxpayers claiming the credits proposed in the bill. Seventy-five percent of corporate tax revenues are distributed to the general fund and 25% are distributed to the TTF. Of the 25% distributed to the TTF, approximately 30% is distributed to local jurisdictions. Based on the maximum amount of credit certificates being issued, local government revenues would decrease by approximately $1.5 million in fiscal 2003 through 2006.

Additional Information

Prior Introductions: None.

Cross File: SB 801 (Senators Hogan and Teitelbaum) – Budget and Taxation.

Information Source(s): Comptroller of the Treasury (Bureau of Revenue Estimates), Montgomery County, Department of Legislative Services

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