

**Department of Legislative Services**  
Maryland General Assembly  
2002 Session

**FISCAL NOTE**

Senate Bill 528 (Senator Ruben, *et al.*) (Montgomery County Administration)  
Budget and Taxation

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**Sales and Use Tax - Exemption - Biotechnology and Internet Infrastructure**

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This bill exempts from the sales and use tax the sale or use of: (1) certain communications equipment for use in an internet infrastructure facility; and (2) certain tangible personal property that is incorporated into biotechnology manufacturing facilities.

The bill takes effect July 1, 2002.

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**Fiscal Summary**

**State Effect:** General fund revenues could decline depending on the number of firms eligible for the sales tax exemption and the level of purchases by these firms of goods that would become exempt. The precise level of such revenue losses cannot be reliably estimated at this time, but could be up to \$40 to \$50 million per year.

**Local Effect:** None.

**Small Business Effect:** Meaningful.

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**Analysis**

**Bill Summary:** The bill's provisions are as follows:

### *Sales and Use Tax Exemption for Internet Infrastructure Facilities*

The sales and use tax would not apply to the sale of communications equipment for use in an internet infrastructure facility.

Communications equipment is defined as equipment and related software, used separately or as part of a system, to receive, store, protect, manage, or transmit information in electro-magnetic form; and any ancillary equipment used to ensure the reliable operation, security, access, authentication, and billing related to communications equipment. Communications equipment includes: computers; firewalls; analog-to-digital or digital-to-analog conversion equipment; modems; disk or tape storage equipment; network management systems; routers; circuit, packet, and optical switches; transmission and receiver equipment; wires and cables; cable termination and signal generation and test equipment; antennas; uninterruptible power supplies; power generators; alarm systems; leasehold improvements; heating, ventilation, and air conditioning systems (HVAC); and fire protection equipment.

“Internet infrastructure facility” is defined as a building or a portion of a building used or intended to be used primarily to provide: (i) interconnection of multiple internet service providers; (ii) interconnection of the internet to telephone lines or other telecommunications connections, either directly or by way of a network; (iii) hosting of content for the internet; or (iv) storage of data that is available to the public internet for real-time download to customers.

The exemption would not apply to the sale of communications equipment to:

- a cable television operator franchised by a political subdivision of the State, or its affiliates or subsidiaries;
- a telephone company, telecommunications carrier, or other company regulated by the public service commission, or its affiliates or subsidiaries;
- a cellular telephone company or its affiliates or subsidiaries; or
- a company that is using the internet infrastructure facility to provide service for itself, its subcontractors, or its affiliates or subsidiaries.

### *Sales and Use Tax Exemption for Biotechnology Manufacturing*

The sales and use tax would not apply to the sale of tangible personal property if the buyer intends to incorporate the tangible personal property into real property at the time of construction, expansion, or renovation of a facility to be used primarily for biotechnology manufacturing. The exemption would apply only to that part of a facility

where the occupant has been certified as a qualified business entity eligible for a Jobs Creation Tax Credit.

Unless otherwise agreed to in writing, if the tangible personal property eligible for a tax exemption is purchased in furtherance of a lease where the tenant has been certified for the Jobs Creation Tax Credit, the lessor would be required to reduce by the amount of the tax exemption received under this provision the amount of taxes or other moneys for which the lessee is contractually liable under the lease agreement. This provision is enforceable only by the lessee and is not intended to create any enforcement responsibility on the part of the State.

To qualify for an exemption under this provision, an owner must file an application for an exemption certificate with the Comptroller. The Comptroller must establish by regulation procedures to allow a person who, because of a contractual obligation, purchases tangible personal property to be incorporated into the real property of an exempt biotechnology facility, to purchase the tangible personal property tax free.

**Current Law:** Purchases of the items covered under this bill are currently subject to a 5% sales and use tax. Certain types of equipment are exempt from the sales and use tax under exemptions for research and development and production activities.

**Background:** SB 792 of 2001, a similar but not identical bill, was referred to interim study by the Senate Budget and Taxation Committee. Legislative Services presented a review of SB 792, and its companion bill, HB 1137 of 2001. Legislative Services examined the application of the sales tax to business firms and discussed the existing business-related sales tax exemptions.

**State Revenues:** The amount of lost sales tax revenues under the bill would depend on how many internet infrastructure facilities or biotechnology manufacturing firms in Maryland are able to take advantage of the exemption and the amount of qualifying purchases for each such firm. The total revenue loss could be significant.

As noted above, at least four categories of internet firms would be eligible for the internet infrastructure exemption and the range of communications equipment that is exempted is quite broad. (Although at least four types of firms, including cable and telephone companies, are not eligible for the exemption.) The amount of any revenue loss cannot be precisely estimated at this time. For illustrative purposes, however, the relevant product categories, and potential revenue losses from each category, are shown below. Additional revenue losses could result in other categories as well. The actual revenue loss will depend on the use of the exemption.

<b>Comptroller's Sales and Use Category</b>	<b>FY 2001 Sales Tax Revenues</b>	<b>Potential Revenue Loss</b>	<b>Revenue Loss (10%)</b>
Computer Hardware/Software	\$334.0 million	1%	\$3.3 million
Electrical and Electronics	48.8 million	5%	2.4 million
Communications	<u>114.8 million</u>	33%	<u>37.9 million</u>
<b>Total</b>	<b>\$497.7 million</b>		<b>\$43.7 million</b>

Numbers may not sum due to rounding.

There would also be revenue losses from the exemption for sales of tangible personal property that is incorporated into real property at the time of construction, expansion, or renovation of a facility to be used primarily for biotechnology manufacturing, where the occupant has been certified as a qualified business entity eligible for a Jobs Creation Tax Credit. The amount of such losses cannot be precisely estimated at this time. It is also not known the extent to which some of these purchases may already be exempt under the research and development or production activity exemptions.

Anecdotally, however, Legislative Services notes that there are over 300 high technology and biotechnology member firms of the Tech Council of Maryland. The following are examples of recent business activities by some of these firms that might qualify for the sales tax exemption. Purchases made by firms such as Celera, Human Genome Sciences, and Institute of Genomic Research used in the expansion of the Maryland facility would qualify. Equipment used to establish Bio-Infomatrix, which could cost more than \$50 million, could qualify. Medimmune recently expanded its manufacturing facility in Frederick at a cost of about \$50 million, much of which could qualify. BioReliance, another firm with Maryland operations, in its 1999 Annual Report stated that it had commitments to spend \$5.1 million on its U. S. manufacturing facility, including leasehold improvements and laboratory equipment. The Department of Business and Economic Development notes that "the construction costs for a biotechnology manufacturing facility can run well over \$30 million, much of which could qualify."

To the extent that: (1) the sales tax exemption generates economic activity that would otherwise have not taken place absent the exemption; and (2) that additional economic activity generates additional sales tax, income tax, or property tax revenue, then there may be some partial offset of the revenue loss. Legislative Services advises, however, that much of this economic activity is likely to have taken place absent the exemption, negating the impact of any indirect tax revenue recoupment.

**State Expenditures:** The Comptroller's Office would incur one-time administrative expenditures of approximately \$2,500 for printing and communications costs to implement the bill.

**Small Business Effect:** Small businesses providing internet infrastructure services or biotechnology products would experience savings from the sales tax exemption from certain large-ticket equipment purchases.

**Additional Comments:** Montgomery County could not provide information for this fiscal note regarding the number of firms in the county, and the corresponding amount of purchases currently subject to the sales tax, that would be eligible for these exemptions.

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### **Additional Information**

**Prior Introductions:** See discussion above for SB 792 of 2001, a similar bill. HB 1137, the companion to SB 792, received an unfavorable report from the House Ways and Means Committee.

**Cross File:** None.

**Information Source(s):** Comptroller's Office, Department of Business and Economic Development, Montgomery County, Department of Legislative Services

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