Department of Legislative Services

Maryland General Assembly
2004 Session

FISCAL AND POLICY NOTE
Revised

House Bill 57 (Delegate Feldman)
Ways and Means

Biotechnology Investment Incentive Act

This bill creates a tax credit by allowing an individual or a corporation to claim a credit against the State income tax or insurance premium tax for investments made in a qualified biotechnology company or venture capital firm. The maximum credit amount available for each calendar year is limited to $12 million.

The bill takes effect July 1, 2004 and applies to all taxable years beginning after December 31, 2003.

Fiscal Summary

State Effect: Revenue decrease of $12 million annually beginning in FY 2006. The distribution of the loss between the general fund and the Transportation Trust Fund (TTF) cannot be reliably estimated. Special fund expenditures increase by approximately $43,000 in FY 2005, which includes one-time tax form changes and computer programming expenditures.

(in dollars)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
GF/SF/FF Rev.	$0	($12,000,000)	($12,000,000)	($12,000,000)	($12,000,000)
SF Expenditure	43,000	0	0	0	0
Net Effect	($43,000)	($12,000,000)	($12,000,000)	($12,000,000)	($12,000,000)

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

Local Effect: Local government revenues would decline as a result of tax credit claims against the corporate income tax. Seventy-six percent of corporate tax revenues is distributed to the general fund, and 24% is distributed to the TTF. Of the 24% distributed to the TTF, approximately 30% is distributed to local jurisdictions.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: The value of the credit is equal to 33% of an eligible investment made in a qualified biotechnology company or venture capital firm during the taxable year. The maximum amount of the credit cannot exceed (1) $100,000 for individuals; (2) $250,000 for corporations; or (3) the tax liability for the tax year. Any unused amount of the credit may be carried forward up to 15 tax years.

An eligible investment is defined as an at-risk investment in exchange for stock or ownership interest. In order to be eligible for the tax credit, an individual or corporation must invest at least $30,000 in a qualifying company or be a part of a group of up to 20 investors that invest at least $250,000 in a qualifying company. In addition, an individual may not have more than a 10% controlling interest in the company, nor be related to the qualifying company as defined by Section 267(B) of the Internal Revenue Code.

A qualifying company can be either a biotechnology company or a venture capital firm. A qualifying biotechnology company is defined as a for-profit entity that (1) is primarily engaged in the research, development, and commercialization of technology related to biological material; (2) has significant operations in the State; (3) and has less than 100 full-time employees. In addition, the biotech company must meet one of the following requirements: (1) is certified as a biotechnology company by the Maryland Technology Development Corporation (TEDCO); (2) has received funding within the past 24 months from any of the following: the Department of Business and Economic Development (DBED), TEDCO, MdBio, Inc., or the Maryland Industrial Partnerships Program; or (3) has been a tenant of a State-funded incubator facility within the previous 24 months.

A qualifying venture capital firm is defined as (1) organized for the purpose of investing in privately-held technology companies; (2) has its principle place of business in Maryland; and (3) has invested at least $2 million in State biotechnology firms in the year the credit is being sought.

By September 15 following the tax year in which the investment was made, a qualified investor must submit a tax credit application to DBED. If the amount of tax credits in any calendar year claimed is greater than $12 million, the value of each credit approved is reduced by the proportion of excess credits claimed.

The credit can be recaptured by the State if the investor sells the ownership interest in the company within two years of the close of the tax year when the credit was approved. The

State can recapture: (1) 100% in the same year; (2) 67% one year after; and (3) 33% from one to two years after.

The bill provides for DBED to administer the tax credit application, approval, and certification processes. In addition, DBED and the Comptroller's Office must adopt regulations to implement the bill.

Current Law: No State tax credit exists for investments made in venture capital or biotechnology companies.

Background: Maryland has a significant biotechnology industry. The State's industry is the third-largest in the country, ranked by number of companies (behind California and Massachusetts). In December 2001, Ernst and Young LLP was commissioned by MdBio, Inc. to conduct a study of the venture capital climate for bioscience in the State. Their analysis concluded that Maryland had a private venture capital funding gap of approximately $50 to $100 million per year, as compared to other states with substantial bioscience industries. The report made the following recommendations to increase bioscience funding: (1) create a State venture capital fund focused on bioscience; (2) increase the amount of State retirement and pension money invested in bioscience companies; and (3) allocate a portion of tobacco settlement money to biotech-related activities.

State Revenues: Credits could begin to be claimed in tax year 2005 (fiscal 2006). If the maximum amount of credits is claimed for each year beginning in tax year 2005, revenues will decrease by $12 million annually beginning in fiscal 2006.

Credits taken against either the insurance premium tax or personal income tax reduce general fund revenues in the amount of the credit claimed. Because 76% of all corporate income tax revenues is distributed to the general fund and 24% is distributed to the TTF, credits taken on corporate income tax returns will reduce those respective funds accordingly. Further, 30% of the 24% of revenue distributed to the TTF is distributed to local governments. At this time, the mix of credits expected to be claimed against the personal income, corporate income, or insurance premium tax cannot be reliably estimated. The maximum loss to the TTF would occur if all of the credits are claimed against corporate income tax. If this occurs, TTF revenues would decrease by $3 million annually beginning in fiscal 2006.

State Expenditures: The Comptroller's Office reports that it would incur a one-time expenditure increase of $43,000 to add the tax credit to the personal income tax form. This includes data processing changes to the SMART income tax return processing and imaging systems, and system testing. DBED has indicated that the bill's requirements could be handled with existing budgeted resources.

Local Revenue Effect: Local government revenues will decline as a result of corporate taxpayers claiming the credits against the corporate income tax. As mentioned previously, the distribution of the claims among the premium tax, individual income tax, and corporate income tax cannot be reliably estimated. The maximum potential decrease in local government revenues would occur if all of the credits were claimed against the corporate income tax. If this occurs, local government revenues would decrease by $864,000 annually beginning in fiscal 2006.

Small Business Effect: There are approximately 310 bioscience companies in Maryland. To the extent that this tax credit attracts additional investments in the biotechnology industry, qualifying venture capital and biotechnology companies that are small businesses could benefit under the bill. Many of Maryland's biotech companies and venture capital companies would not be considered small businesses (50 employees or less although the bill restricts the eligible biotechnology firms to those with fewer than 100 full-time employees).

Small businesses in other industries could be at a competitive disadvantage in attracting investments to the extent that the tax credit causes investments to shift to the biotech industry.

Additional Information

Prior Introductions: None.

Cross File: SB 124 (Senator Forehand) – Budget and Taxation.

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

Fiscal Note History: First Reader - January 30, 2004
mam/mdr Revised - Clarification - February 25, 2004

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