

Department of Legislative Services
Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE
Revised

House Bill 664
Ways and Means

(Delegate Feldman, *et al.*)

Budget and Taxation

Biotechnology Investment Incentive Act

This bill creates a tax credit against the State income tax for individuals, corporations, and venture capital firms that invest in qualified biotechnology firms. The value of the credit is equal to 50% of an eligible investment made in a qualified biotechnology company during the taxable year. The maximum amount of the credit cannot exceed (1) \$50,000 for individuals; and (2) \$250,000 for corporations and venture capital firms. A taxpayer claiming the credit can claim a refund in the amount by which the credit exceeds the tax liability in the year. The bill establishes an application and certification procedure and creates a reserve fund to which the Governor must appropriate funds. The amount of credits that the Department of Business and Economic Development (DBED) can award in each fiscal year cannot exceed the amount of money in the fund.

The bill takes effect July 1, 2005 and applies to tax year 2005 and beyond.

Fiscal Summary

State Effect: Potential significant general fund expenditure in FY 2007 and beyond. The amount of the expenditure depends on the amount of money appropriated to the reserve fund in each year. General fund expenditures would increase by approximately \$44,400 in FY 2007 due to one-time tax form changes and computer expenditures. Potential significant increase in general fund revenues in FY 2007 and beyond and corresponding decrease in Transportation Trust Fund (TTF) revenues due to reserve fund transfers for credits claimed against the corporate income tax.

Local Effect: Local government revenues would decrease as a result of tax credit claims against the corporate income tax. Corporate income tax revenue is distributed 76% to the general fund, and 24% to the TTF. Of the 24% distributed to the TTF, approximately 30% is distributed to local jurisdictions in the form of local highway user revenues. No effect on expenditures.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: 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. DBED is required to submit a report to the Governor and the General Assembly detailing specified information about the tax credit by January 10 of each year.

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 must invest at least \$25,000 in a qualifying company and a corporation must invest at least \$250,000 in a qualifying company.

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, or commercialization of technology related to biological material; (2) has been in business less than 10 years; (3) has less than 50 full-time employees; (4) has its headquarters and base principal place of operations in Maryland; (5) is certified as a biotechnology company by DBED.

A qualifying venture capital firm is defined as (1) organized for the purpose of investing in privately-held technology companies; (2) has its principal place of business in Maryland; (3) has at least one year of experience investing in biotech or biopharmaceutical companies; (4) has two principals that each have at least five years of venture capital experience; and (5) has at least one principal that has invested at least \$5 million in Maryland biotechnology companies.

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 creates a Maryland biotechnology investment tax credit reserve fund. The total amount of initial credit certificates issued by DBED in each fiscal year cannot exceed the amount appropriated to the reserve fund in the State budget. The bill requires the Governor to include an appropriation to the reserve fund in each budget bill. The bill does not require or specify a recommended amount that is to be appropriated to the fund. The Governor may not reduce an appropriation to the reserve fund that is approved by the

General Assembly. For each fiscal year, if funds are transferred from the reserve fund as a result of any law, the amount of total credits that can be approved by DBED is reduced by the amount of money transferred. If funds to the reserve fund are not expended in a fiscal year, any unexpended amount can be used in the next fiscal year.

The bill requires DBED to approve applications based on the order in which they were received. Within 30 days of making a qualifying investment, the individual or business must submit an application to DBED. Within 30 days of receiving the application, DBED would issue an initial credit certificate based on the estimated investment in a biotechnology company. The business or investor must invest in the biotechnology company within 30 days after receiving an initial credit certificate and notify DBED of the investment within 10 days of investing in a biotechnology company. DBED would then issue a final credit certificate based on the actual amount of the qualifying investment.

Within 15 days of each calendar quarter, DBED is required to notify the Comptroller the total number of credits that were certified during the quarter, the total amounts of the maximum credit amount stated in the initial credit certificates, and the total amounts of final certified credit amount. Upon this notification from DBED, the Comptroller is required to transfer from the reserve fund to the general fund the total amounts stated in the final credit certificates that were certified during the calendar quarter.

Tax credits can be claimed beginning in tax year 2007.

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

State Fiscal Effect:

Appropriations to the Reserve Fund

The bill provides that the Governor appropriate funds to the reserve fund in the budget bill. The bill does not require or suggest an amount that should be appropriated. It is assumed that the earliest an appropriation can be made is in fiscal 2007.

Revenue Effects from Reserve Fund Transfers

The bill requires the Comptroller to transfer money from the reserve fund to the general fund an amount that is anticipated to offset credits that would be claimed during the fiscal year. Twenty-four percent of corporate income tax revenue is distributed to the TTF. All the money transferred from the reserve fund by the Comptroller in anticipation of credits being claimed is to be deposited in the general fund and losses to the TTF would not be

offset. As a result, general fund revenues would increase and TTF revenues would decrease by a corresponding amount in fiscal 2007 and beyond. The amount depends of the amount of credits claimed against the corporate income tax and cannot be reliably estimated.

It is also assumed that taxpayers claim the credit in the tax year that corresponds to the fiscal year in which the Comptroller transfers funds to the general fund on notification of a certified credit. To the extent that taxpayers claim the credit in a tax year or adjust estimated quarterly payments or withholdings in a different fiscal year in which the transfer is made, general fund revenues could increase in these fiscal years and potentially decrease by a corresponding amount in later fiscal years. This timing issue, however, does not alter the total cost of the bill.

Administrative Expenses

The Comptroller's Office reports that it would incur a one-time expenditure increase of \$44,400 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 reports that it could administer the tax credit program within existing budgeted resources.

Small Business Effect: Small businesses that meet the bill's requirements and qualify for tax credits will benefit from the bill. There are approximately 310 bioscience companies in Maryland. To the extent that this tax credit attracts additional investments in the biotechnology industry, qualifying 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. 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 620 (Senator Forehand, *et al.*) – Budget and Taxation.

Information Source(s): Department of Legislative Services

Fiscal Note History: First Reader - February 23, 2005
ncs/hlb Revised - House Third Reader - April 5, 2005
Revised - Clarification - April 6, 2005
Revised - Enrolled Bill - May 5, 2005
Revised - Clarification - May 23, 2005

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