SB 218

Department of Legislative Services
Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE

Senate Bill 218 (The President, *et al.*)
(By Request – Administration)

Budget and Taxation

Business and Economic Development - Entrepreneurial Investment Technology Tax Credit

This Administration bill creates a tax credit for investments made in qualified technology companies. The amount of credit is equal to 45% of qualified investments made after January 1, 2005; not to exceed $100,000 per investment and $200,000 in any tax year. The bill provides for a certification process that is administered by the Department of Business and Economic Development (DBED). The maximum credit amount available for each fiscal year is limited to $8 million.

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

Fiscal Summary

State Effect: General fund revenues would decrease by approximately $2.7 million in FY 2009 due to credits being claimed according to provisions specified by the bill. General fund revenues would decrease by approximately $5.3 million in FY 2010. Phased-in claiming of the credit would result in annual loss of $8.0 million in FY 2011 and beyond. Special fund expenditures would increase by approximately $84,400 in FY 2006, which includes one-time tax form changes and computer programming expenditures.

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
GF Revenue	$0	$0	$0	($2.7)	($5.3)
SF Expenditure	.1	0	0	0	0
Net Effect	($.1)	$0	$0	($2.7)	($5.3)

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

Local Effect: None.

Small Business Effect: The Administration has determined that the bill will have a meaningful impact on small business. (attached) Legislative Services concurs with the assessment that the bill will have a meaningful impact as discussed below.

Analysis

Bill Summary: A taxpayer may not claim any portion of the tax credit until three years after the tax year in which the investment was made. At this time, the taxpayer can claim a maximum of one-third of the credit in each of the first three tax years. The bill provides that an investor is required to claim at least a portion of the credit within five taxable years after the tax year in which the investment was made. Any unused amount of the credit can be carried forward five years from the taxable year in which the investor first claims any portion of the tax credit. In order to claim the credit, the taxpayer must submit specified information including whether the qualified technology company in which the taxpayer invested is still operating to DBED annually by June 30 of each year.

An eligible investment is defined as an at-risk investment and includes funds provided in exchange for (1) an equity interest in the business; (2) a debt instrument convertible to an equity interest; and (3) an agreement to receive specified revenues generated by the business. In order to be certified as a qualified investor, an applicant must submit the following information to DBED: (1) specified information about the business into which the investment will be made; (2) the details of the investment; and (3) any other information about the qualified business DBED requires. In addition, DBED may require that information provided be verified by an independent auditor provided by and paid for by the investor.

The bill requires that in order to be certified as a qualified investor, the investor must: (1) own and invest at least $200,000 under active financial management; (2) agree to invest a minimum of $50,000 in a qualified technology business; (3) not own or control more than 20% of the qualified technology business after the proposed investment; (4) not be a founder, officer, member of, or hold similar positions in the technology business; (5) notify DBED of intent to seek certification before the investment is made; and (6) have a personal net worth of at least $1 million. The equity in an individual's primary residence cannot be included in the person's net worth.

The bill provides for DBED to administer the tax credit application, approval, and certification processes. In addition, DBED may adopt regulations to implement the bill.

Current Law: No similar State tax credit of this type exists.

State Revenues: Credits could be earned for investments made beginning in 2005. The bill provides that credits for these investments could be claimed no earlier than in tax year 2008, and at a maximum amount in each year equal to one-third of the credit. As a result, general fund revenues would decrease by approximately $2.7 million in fiscal 2009 and $5.3 million in fiscal 2010 and beginning in fiscal 2011 $8.0 million annually. This estimate is based on the following facts and assumptions:

- DBED will certify the maximum amount of $8 million in each fiscal year; and
- taxpayers will claim the credit in the maximum amount allowed by the bill in each tax year.

To the extent that taxpayers carry forward credits and do not claim the maximum amount as provided by the bill, revenue losses would be less in fiscal 2009 and 2010 but would be correspondingly greater in the out-years and could be greater than $8.0 million in fiscal 2011 and beyond. In addition, the bill does not provide a limitation on the amount of credit that can be claimed after the limits placed in the first five tax years after the qualified investment was made.

State Expenditures: The Comptroller's Office reports that it would incur a one-time expenditure increase of $84,400 to add the tax credit to the personal income tax form and to meet the requirements of the bill that the Comptroller notify DBED information specified by the bill. 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.

Small Business Effect: The Department of Legislative Services agrees with the Administration's small business impact assessment and adds that small businesses that qualify for investments and claim the proposed credit would benefit under the bill.

Additional Information

Prior Introductions: None.

Cross File: HB 249 (The Speaker, *et al.*) (By Request – Administration) – Ways and Means.

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

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mp/hlb

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