Department of Legislative Services
Maryland General Assembly
2006 Session

FISCAL AND POLICY NOTE

House Bill 834 (Delegate Feldman)
Ways and Means

Income Tax - Maryland Biotechnology 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 (R&D) tax credits or unused net operating losses to sell those benefits to a corporation.

The bill takes effect July 1, 2006 and applies to tax year 2007 and beyond. The bill terminates December 31, 2010.

Fiscal Summary

State Effect: General fund revenues would decrease by $15.2 million and Transportation Trust Fund (TTF) revenues would decrease by $4.8 million in FY 2008 through 2011 assuming that the maximum credit certificates are issued each year. Expenditures would not be affected.

($ in millions)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
GF Revenue	$0	($15.2)	($15.2)	($15.2)	($15.2)
SF Revenue	0	(4.8)	(4.8)	(4.8)	(4.8)
Expenditure	$0	$0	$0	$0	$0
Net Effect	$0	($20.0)	($20.0)	($20.0)	($20.0)

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

Local Effect: Local highway user revenues distributed from the TTF would decrease by approximately $1.4 million annually in FY 2008 through 2011. Expenditures would not be affected.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: DBED may not approve the transfer of more than $20 million of tax benefits for any fiscal year. A corporation may surrender a maximum of $4 million in tax benefits during the program.

An eligible biotechnology company may apply to DBED to transfer tax benefits under the program. In order to qualify, the biotechnology company must: (1) have significant operations in the State; (2) have fewer than 225 employees; (3) be engaged in the research, development, production, or provision of biotechnology for the purpose of developing or providing products or processes for specific commercial or public purposes. Corporations must apply to DBED in order to receive transferable tax benefits. All applications must be received by June 30 prior to the beginning of the fiscal year in which the benefit will be transferred.

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, including: (1) an evaluation of the biotechnology company's actual or potential scientific and technological viability; (2) a determination that the biotechnology company's principal products or services are sufficiently innovative to provide a competitive advantage; (3) a determination that the 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 demonstrates the prospect of a significant positive change in the biotechnology company's net income.

A 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.

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.

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 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 and may include provisions for: (1) payment of processing fees; (2) allocation of tax benefits if more than $20 million in applications are received in a fiscal year; and (3) transfer of bundled tax benefits.

Current Law: No similar State tax credit exists.

Background: Chapters 515 and 516 of 2000 established the R&D income tax credit. Businesses that incur qualified research and development expenses in Maryland are entitled to the credit. The total credits approved may not exceed $6 million in a tax year. In five years of the program, a total of $30 million in credits have been awarded.

Chapter 99 of 2005 established the biotechnology investment tax credit program. A tax credit against the State income tax is available 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 proposed fiscal 2007 budget provides $6 million in tax credits for the program.

State Revenues: The bill provides that DBED can award a maximum of $20 million in credits in each fiscal year. If the maximum $20 million in credit certificates were issued each year, general fund revenues would decrease by $15.2 million and TTF revenues would decrease by $4.8 million in fiscal 2008 through 2011 due to the distribution of corporate income tax revenues.

Small Business Effect: 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.

Additional Information

Prior Introductions: Similar bills were introduced in the 2002 and 2001 sessions. SB 431 of 2002 was withdrawn. SB 801 of 2001 was referred to interim study by the Senate Budget and Taxation Committee. HB 1098, its companion bill, received an unfavorable report from the House Ways and Means Committee.

Cross File: SB 954 (Senator Jones) – Budget and Taxation.

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

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