Department of Legislative Services
Maryland General Assembly
2015 Session

FISCAL AND POLICY NOTE

Senate Bill 584 (Senator Pugh, *et al.*)
Budget and Taxation

Income Tax - Angel Investor Tax Credit Program

This bill creates a tax credit against the State income tax for investors that make qualified investments in Maryland innovation businesses. The nonrefundable credit is equal to 50% of the qualified investment, not to exceed $50,000 for an individual or $100,000 for married couples that file a joint return or a pass-through entity. The amount of credits that the Department of Business and Economic Development (DBED) can award each year cannot exceed the amount of money appropriated to a reserve fund established by the bill.

The bill takes effect July 1, 2015, and applies to tax year 2015 and beyond.

Fiscal Summary

State Effect: Potential significant general fund expenditure increase beginning in FY 2016. The amount of the expenditure increase depends on the amount of money, if any, appropriated to the reserve fund each year. If the credit is funded at $5.0 million, general fund expenditures increase by $5.0 million annually. Administrative costs increase by $111,800 in FY 2016 and by $89,700 in FY 2020. Revenues are not affected.

($ in millions)	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020
Revenues	$0	$0	$0	$0	$0
GF Expenditure	5.1	5.1	5.1	5.1	5.1
Net Effect	($5.1)	($5.1)	($5.1)	($5.1)	($5.1)

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

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: The bill establishes a Maryland Angel Investor Tax Credit Reserve Fund. The total amount of tax credit certificates issued by DBED in each fiscal year cannot exceed the amount appropriated to the reserve fund in the State budget. It is the General Assembly's intent that the Governor appropriate at least $5.0 million to the reserve fund in each year. Any amount of money in the fund that is not expended in the fiscal year is rolled over into the next fiscal year.

The credit is claimed by a qualified investor who (1) meets the qualifications of the bill; (2) follows the application and certification process established by the bill; and (3) invests in a qualified innovation business that is certified by DBED.

A qualified investor can claim a nonrefundable credit equal to 50% of the investment, not to exceed $50,000 for an individual or $100,000 for a pass-through entity or a married couple that files a joint return. DBED may not certify investments in a single qualified innovation business that total more than 15% of the total appropriations to the reserve fund for that fiscal year. DBED must reserve at least 10% of the total appropriation to the reserve fund in each fiscal year for tax credits for investments in qualified innovation businesses that are women-, minority-, or veteran-owned businesses. An eligible investment is defined as an at-risk investment of at least $10,000 ($20,000 for a pass-through entity or joint filer) in exchange for stock, convertible debt, or ownership interest. An investor may not acquire an ownership interest in a company that exceeds 20% and must submit an application to DBED.

A qualified innovation business is defined as a for-profit entity that has or is in the process of developing a technology, product, or service that is unique and legally owned or licensed by the business. A qualified innovation business does not include a qualified biotechnology company or a qualified cybersecurity company. A qualified innovation business must be in good standing as determined by the State Department of Assessments and Taxation (SDAT) and meet specified criteria, including requirements that the company (1) does not have annual revenue of more than $5 million; (2) has been in business for no more than five years; (3) has not received more than $3 million in investments; (4) has less than 35 full-time employees; (5) has its headquarters and base of operations in Maryland; (6) is not publicly traded on any exchange; and (7) has at least 51% of its full-time equivalent employees employed in the State and at least 51% of its payroll paid to the employees in the State.

Tax credit applications are approved on a first-come, first-served basis until the total cap for the year is reached. The bill provides for the circumstances under which the credit may be rescinded, revoked, or recaptured.

DBED is required to (1) approve tax credit applications; (2) determine the eligibility of qualified innovation businesses and investors; and (3) adopt regulations, in consultation with the Comptroller, to implement the credit. Additionally, the bill adds the Angel Investor tax credit to the list of economic development programs that DBED must report on to the Governor and the General Assembly each year.

Current Law: Chapter 99 of 2005 established the biotechnology investment tax credit, which offers a similar refundable tax credit for investments in qualified biotechnology companies. DBED administers the tax credit application, approval, and certification process and is required to submit a report to the Governor and the General Assembly detailing specified information about the tax credit each year. An investor who invests at least $25,000 in a qualified Maryland biotechnology company can claim a credit equal to 50% of the investment, not to exceed $250,000. DBED may not certify investments in a single biotechnology company that total more than 15% of the total appropriations to the reserve fund for that fiscal year.

Chapter 390 of 2013 established a refundable tax credit for investments in qualified cybersecurity companies. DBED administers the tax credit application, approval, and certification process and is required to submit a report to the Governor and the General Assembly detailing specified information about the tax credit each year. A qualified Maryland cybersecurity company can claim a credit equal to 33% of a qualified investment, not to exceed $250,000. A qualified investment is an at-risk investment of at $25,000 in exchange for stock or ownership interest. DBED may not certify investments in a single cybersecurity company that total more than 15% of the total appropriations to the reserve fund for that fiscal year.

Background: There are currently 5,758 firms certified as a Minority Business Enterprise (MBE) and/or a Disadvantaged Business Enterprise in the State. The State's MBE program requires that a statewide goal for MBE contract participation be established biennially through the regulatory process under the Administrative Procedure Act.

The Veteran-Owned Small Business Enterprise program has a goal of awarding at least 0.5% of total procurement spending to small businesses owned and operated by veterans. Eligible businesses must be verified as veteran-owned small businesses by the U.S. Department of Veterans Affairs' Center for Veterans Enterprise (CVE). Under the program, agencies have to establish an expected degree of veteran-owned small business participation for each procurement, based on the potential subcontracting opportunities and the availability of veteran-owned small businesses to respond competitively to the solicitation. The VetBiz.gov registry maintained by CVE lists 514 verified veteran-owned small businesses in Maryland that are eligible to participate in the program, more than double the number when the program was enacted in 2010.

State Fiscal Effect:

Appropriations to the Reserve Fund

It is the intent of the General Assembly that the Governor appropriate at least $5.0 million to the reserve fund in each year. Assuming the program is funded at this level, general fund expenditures will increase by $5.0 million annually. To the extent that the Governor provides less or no money to the reserve fund in any year, the increase in general fund expenditures will be less. To the extent that the Governor provides more than $5.0 million to the reserve fund in any year, the increase in general fund expenditures will be greater.

Revenue Impacts

Within 15 days after the end of each calendar quarter, DBED is required to notify the Comptroller of the total amount of final credit certificates that were issued during the quarter. Upon this notification, 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 issued during the quarter.

It is 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 or adjust estimated quarterly payments or withholdings in a different fiscal year from when 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 overall cost of the bill.

Administrative Expenditures

General fund expenditures increase by $111,772 in fiscal 2016 due to implementation costs at DBED and the Comptroller's Office, as described below. SDAT can issue letters of good standing for qualified innovation businesses with existing resources.

The Comptroller's Office reports that it will incur a one-time expenditure increase of $30,960 in fiscal 2016 to add the credit to the personal income tax form. This amount includes data processing changes to the SMART income tax return processing and imaging systems and systems testing.

DBED indicates it would need one tax credit specialist to administer the program. General fund expenditures will increase by an estimated $80,812 in fiscal 2016, which reflects the bill's July 1, 2015 effective date. This estimate includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Position	1
Salary and Fringe Benefits	$75,942
Other Operating Expenses	4,870
DBED Expenditures	**$80,812**
Comptroller Expenditures	**30,960**
Total FY 2016 Expenditures	**$111,772**

Future year expenditures reflect a full salary with annual increases and employee turnover as well as annual increases in ongoing operating expenses.

Small Business Effect: Small businesses that are pass-through entities and make qualified investments in a qualified innovation business may benefit by claiming a nonrefundable tax credit against the individual income tax of up to $100,000. Qualified innovation businesses that have developed or are in the process of developing a technology, product, or service that is unique and legally owned or licensed by the business may benefit by increased investments from qualified investors.

Additional Information

Prior Introductions: None.

Cross File: HB 789 (Delegate Lierman, *et al.*) - Ways and Means.

Information Source(s): State Department of Assessments and Taxation, Department of Business and Economic Development, Department of Budget and Management, Comptroller's Office, Department of Legislative Services

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Analysis by: Heather N. Ruby

Direct Inquiries to:
(410) 946-5510
(301) 970-5510