

REVENUE ESTIMATING CONFERENCE

TAX: Corporate Income Tax

ISSUE: Credit for Research and Development

BILL NUMBER(S): HB 733/SB1398

SPONSOR(S): Representative Grant

MONTH/YEAR COLLECTION IMPACT BEGINS: July 1, 2008

DATE OF ANALYSIS: February 5, 2008

SECTION 1: NARRATIVE

a. **Current Law:** N/A

b. **Proposed Change:** Addition of a Florida R&D Tax Credit to Corporate Income Tax

SECTION 2: DESCRIPTION OF DATA AND SOURCES

Proposed bill

Internal Revenue Code Section 42: Credit for Increasing Research Activities

IRS Form 6765 Credit for Increasing Research Activities

Internal Revenue Service Briefing Paper on Taxpayer Approaches to Capturing Costs for the Research Credit

2004 Corporation Returns Report (IRS)

2003 Corporation Returns (IRS) Number of Returns, Selected Items from Form 6765...(Three Tables)

The Mechanics of California's R&D Tax Credit.

State of California Form 3523 Research Credit (And Instructions)

State of Illinois 35 ILCS 5/201 (k) Research and development credit

State of Georgia § 48-7-40.12.

State of Georgia Form IT-RD (6/01)

The Research and Development Tax Credit for Georgia

Report to the Pennsylvania General Assembly on the Research and Development (R&D) Tax Credit March 15, 2000

Report to the Pennsylvania General Assembly on the Research and Development (R&D) Tax Credit March 15, 2007

SECTION 3: METHODOLOGY (INCLUDE ASSUMPTIONS AND ATTACH DETAILS)

A. Differences between HB 733 and SB 1398

HB 733 states that the act defines the term “qualified research expenses.” SB 1398 does not state that the act defines this term.

Neither bill provides a definition of “qualified research expenses.”

HB 733 provides additional detail. These details are addressed further on in both bills.

There are a number of differences in paragraph (1) (Intent in the Senate Bill); however, none of these differences should impact the estimate.

HB 733 includes the phrase “calculation is subparagraph 1. by the average of the business” between the words “the” and “enterprise’s” in SB 1398. Without this phrase, the equation does not make sense.

SB 1398 uses letters (a) through (e), where HB 733 uses numbers (4) through (8). Therefore, paragraph (4) in SB 1398 is paragraph (9) in HB 733. In this discussion, I will reference the HB 733 numbers.

(8) HB 733 caps the credit at \$15 million, whereas SB1398 caps the credit at \$__ million.

For the most part, the other differences are stylistic; however, HB 733 specifies some parts more than SB 1398. For example (HB 733 additions in **bold**)

(3) ... under s.41 of the Internal Revenue Code **of 1986, as amended.**

(7) ... the Department **of Revenue**... ... must use the **newly obtained research and development** tax credit... ... assigned **research and development** credit...

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B. Issues with and Assumptions to HB 733

The term “research and development expenditures” is not defined. (2)(a)1.

The term “research and development expenses” is not defined. (2)(a)2.

The term “qualified research expenses” is not defined. (3)

It is assumed that the terms “research and development expenditures, research and development expenses,” and “qualified research expenses” are all defined as “Qualified research expenses,” as defined in Section 41(b)(1) of the Internal Revenue Code of 1986, as amended.

The scale (Florida, U.S., or worldwide, subsidiary or corporate) is not stated. (2)(a)1.&2.

Both “research and development expenditures” and “gross receipts” are assumed to be defined at the worldwide level.

The “predetermined base period” is not defined. (2)(a)1.

It is assumed that the ending date of the “predetermined base period” would be late enough so as some companies could qualify and the cap on the credits will be met. It is also assumed that the ending date of the “predetermined base period” would be early enough so as credits could be awarded in the first year.

It is assumed that the “base amount” will be relatively small and that “excess-over-base” will be close to the actual research and development expenditures in Florida.

There is no definition given for “engaged in” or any of the types of businesses listed. (2) (b)

It is assumed that the method for determining a company’s business sector can be made in rule, and this process will not retard the process of awarding the credits.

It is not clear if the term “credit taken” means that the “credit is used” against the tax liability or if it means that the “credit is acquired” so as to be used, carried forward or sold. (5)

It is assumed that the 50 percent limitation is based on the credits used by the company doing the research and development. The company could have residual credits in the given year that could be carried over or sold.

As written, an assigned or sold research and development credit could be used to offset 75 percent of any tax (not just corporate income tax) liability. Unlike the earning of the credit, it appears that the credits may be purchased by any taxpayer, regardless of business sector. The 75 percent limitation maybe *prior to*, not necessarily *after*, all other credits have been applied [as in (5)]. (7)

It is assumed that language will be added to restrict the tax liability to Florida corporate income tax. It is also assumed that all Florida corporate income tax payers, regardless of business sector, will be eligible to purchase and use these credits.

It is unclear if the limit (cap) is based on individual companies or statewide collections. It is also unclear if the limitation is based on the incurrence the credit or the redemption of the credit. (8)

It is assumed that the limit would be structured in the same way as in the Pennsylvania rule. It is

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assumed that the there will be a similar demand for these credits in Florida as they are in Pennsylvania.

C. Additional Assumptions

It is assumed that the Department of Revenue will be able to adopt rules, etc. in time to distribute the credits in SFY 2008-09.

It is assumed that all available \$15 million in credits will be applied for each year. The high estimate assumes that the credits will all be used in the year they are awarded. The low estimate assumes that the credits will be used and carried over in a similar proportion as in Pennsylvania.

SECTION 4: PROPOSED FISCAL IMPACT

| State Impact—All Funds | FY 2008-09 Annualized | FY 2008-09 Cash | FY 2009-10 Cash |
|------------------------|-----------------------|-----------------|-----------------|
| High | (\$15 million) | (\$15 million) | (\$15 million) |
| Middle | (\$15 million) | (\$7.5 million) | (\$15 million) |
| Low | (\$15 million) | (\$0.2 million) | (\$5.7 million) |

| State Impact—All Funds | FY 2010-11 Cash | FY 2011-12 Cash |
|------------------------|------------------|-----------------|
| High | (\$15 million) | (\$15 million) |
| Middle | (\$15 million) | (\$15 million) |
| Low | (\$11.1 million) | (\$15 million) |

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SECTION 5: CONSENSUS ESTIMATE (ADOPTED 2 / 8 / 08) The conference adopted the middle estimate.

| | FY 2008-09 Annualized | FY 2008-09 Cash | FY 2009-10 Cash |
|--------------------|-----------------------|-----------------|-----------------|
| General Revenue | (15.0) | (7.5) | (15.0) |
| State Trust | | | |
| Total State Impact | | | |
| Total Local Impact | | | |
| Total Impact | (15.0) | (7.5) | (15.0) |

| | FY 2010-11 Cash | FY 2011-12 Cash |
|--------------------|-----------------|-----------------|
| General Revenue | (15.0) | (15.0) |
| State Trust | | |
| Total State Impact | | |
| Total Local Impact | | |
| Total Impact | (15.0) | (15.0) |

Pennsylvania (Actual)

| | Totals | Percent Utilized | Annual Percent |
|------------------------------|--------------|------------------|----------------|
| 2006 Credits Awarded | \$40,000,000 | 1.57% | 1.57% |
| 2006 Credits Utilized | \$627,919 | | |
| 2004 & 2005 Credits Awarded | \$60,000,000 | 74.06% | 36.24% |
| 2004 & 2005 Credits Utilized | \$44,433,044 | | |
| Residual | | 25.94% | 25.94% |

Florida (Estimate)

| | Credits Used in SFY 08-09 | | Credits Used in SFY 09-10 | | Credits Used in SFY 10-11 | | Credits Used in SFY 11-12 | | |
|------------------------------|---------------------------|------------------|---------------------------|------------------|---------------------------|------------------|---------------------------|------------------|---------------|
| | Credits Awarded | Percent Utilized | Credits Used | Percent Utilized | Credits Used | Percent Utilized | Credits Used | Percent Utilized | Credits Used |
| Credits Awarded in SFY 08-09 | \$15.0 | 1.57% | \$0.2 | 36.24% | \$5.4 | 36.24% | \$5.4 | 25.94% | \$3.9 |
| Credits Awarded in SFY 09-10 | \$15.0 | 0.00% | \$0.0 | 1.57% | \$0.2 | 36.24% | \$5.4 | 36.24% | \$5.4 |
| Credits Awarded in SFY 10-11 | \$15.0 | 0.00% | \$0.0 | 0.00% | \$0.0 | 1.57% | \$0.2 | 36.24% | \$5.4 |
| Credits Awarded in SFY 11-12 | \$15.0 | 0.00% | \$0.0 | 0.00% | \$0.0 | 0.00% | \$0.0 | 1.57% | \$0.2 |
| Totals | | | \$0.2 | | \$5.7 | | \$11.1 | | \$15.0 |