

**INDIVIDUAL INCOMETAX  
CORPORATE FRANCHISE TAX  
Refundable R & D Tax Credit  
Subtraction: Technology Investments**

March 30, 2001

	<b>Yes</b>	<b>No</b>
Separate Official Fiscal Note Requested		<b>X</b>
<b>Fiscal Impact</b>		
DOR Administrative Costs/Savings	<b>X</b>	

Department of Revenue  
Analysis of S.F. 2024 (S. Kelley)

	<u>Revenue Gain or (Loss)</u>			
	<u>F.Y. 2002</u>	<u>F.Y. 2003</u>	<u>F.Y. 2004</u>	<u>FY2005</u>
		(000's)		
Individual Income Tax		----(Unknown*)----		
Corporate Franchise Tax	(\$1,600)	(\$1,300)	(\$1,500)	(\$1,700)
General Fund Total		----(Unknown)----		

\*Likely to be small through fiscal year 2005

For the individual income tax, effective for investments made after December 31, 2000.  
For the corporate franchise tax, effective for tax years beginning after December 31, 2000.

**EXPLANATION OF THE BILL**

**Current Law:** For the individual income tax, capital gains are included in income to the same extent as under federal law.

The research and development tax credit is a nonrefundable credit allowed against the corporate franchise tax, and it has a fifteen-year carryover provision.

**Proposed Law:** For the individual income tax, a subtraction would be allowed equal to 50% of the capital gain included in federal taxable income from investments in qualified high technology businesses. A business qualifies if at least 50% of its activities consists in conducting qualified research in Minnesota or it derives at least 50% of its income from performing such research in Minnesota. The research qualifies if it is the type that qualifies for the federal research credit under IRC Sec. 41(d) or meets the definition provided regarding computer software. Certain types of companies are specifically excluded.

The research and development credit would be made refundable, and the carryover provision would be repealed.

## REVENUE ANALYSIS DETAIL

### *Individual Income Tax*

- Because the subtraction is effective for investments made after December 31, 2000, there will be no impact until investments made in 2001 and after are sold and a gain realized. Therefore, it is expected that any impact in fiscal years 2002 through 2005 would be small. The impact could be significant beyond fiscal year 2005.
- The criteria for a “qualified high technology business” are such that they would limit the number of eligible businesses. Only investments in these businesses would be allowed the special capital gains treatment in the bill.
- The amount eligible for the proposed subtraction in the future cannot be determined at this time. The market environment for high technology firms is extremely uncertain and cannot be predicted with any validity.
- A single lucrative sale could generate considerable gains to be excluded, but such unique events cannot be forecast.

### *Corporate Franchise Tax*

- The revenue estimate is based on data from returns received in calendar year 1998.
- The estimate assumes that filed 1998 data represents collections in fiscal year 1998.
- Filed 1998 R & D tax credit data was examined to determine how much of the current law R & D tax credit would be refundable.
- The average growth in R & D credits claimed during the past years is used to project future revenue losses.
- The FY 2002 estimate was increased by 30% to reflect the January 1, 2001, effective date.
- The revenue loss estimate was adjusted to reflect the current law change in weighting of the apportionment factors to 12.5% property, 12.5% payroll and 75% sales, effective for tax years beginning after December 31, 2000.

### **Number of Taxpayers Affected:**

About 75 corporate taxpayers would benefit from making the research and development credit refundable. About 200 corporations that claim the credit would receive no additional benefit.

## ADMINISTRATIVE/OPERATIONAL IMPACT

Because the department is currently formalizing a reengineered process for the income tax, the operational impact of this provision cannot be precisely estimated. However, there will be some additional costs associated with this new subtraction for individuals and a new credit for corporations. See fiscal note for SF 501.

Source: Minnesota Department of Revenue  
Tax Research Division  
<http://www.taxes.state.mn.us/polic.html#analyses>