

MINNESOTA • REVENUE

VARIOUS TAXES

Biotechnology and Health Sciences Zone

April 14, 2003

Department of Revenue

Analysis of H.F. 1183 (Osterman) 1st Engrossment

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

	Revenue Gain or (Loss)			
	<u>F.Y. 2004</u>	<u>F.Y. 2005</u>	<u>FY2006</u>	<u>FY2007</u>
		(000's)		
Property Tax Refund	0	\$0	\$0	(\$14)
Corporate Franchise Tax Exemption	0	(\$30)	(\$70)	(\$120)
General Sales & Use Tax Exemption	0	(\$970)	(\$2,050)	(\$2,260)
General Fund Total	\$0	(\$1,000)	(\$2,120)	(\$2,394)

Biotechnology zone definitions and development plans effective the day following enactment.

Sales tax exemption effective for sales made on or after the day following enactment.

Motor vehicle sales tax exemption effective for sales made after December 31, 2003.

Corporate franchise tax exemption effective beginning with tax year 2004.

Individual income tax exemption effective beginning with tax year 2004.

Property tax exemption effective beginning with property taxes payable in 2005.

EXPLANATION OF THE BILL

Current Law: There are no provisions for a biotechnology and health sciences industry zone in Minnesota. Some tax exemptions and credits are available in border city zones.

Proposed Law: The Commissioner of Trade and Economic Development would designate one biotechnology and health sciences industry zone. Priority must be given to applicants with a development plan that links a higher education/research institution with a biotechnology and health sciences industry facility. A biotechnology and health sciences industry zone must be located within the boundaries of the local unit(s) of government that request the zone.

A zone may not exceed 5,000 acres and may consist of one or more noncontiguous subzones. The designation of the zone would take effect January 1, 2004, and the maximum duration of a zone is twelve years.

EXPLANATION OF THE BILL (cont.)

The bill defines “qualified business” as a person carrying on a trade or business at a place of business located within a biotechnology zone. A business that relocates to a biotechnology zone can qualify if it increases full-time employment by at least 20% in the first full year of operation in the zone, or if it makes a capital investment equivalent to 10% of the gross revenues for the year immediately preceding the taxable year.

Property Tax Exemption: Class 3 commercial, industrial, and utility property in a zone would be exempt from the local property tax and the state general levy if the occupant of the property is a qualified business. The exemption would apply to improvements to real property and to personal property; it would not include land. The exemption does not apply to debt service levies or similar levies to pay general obligation bonds if the bonds were issued before the zone is designated. It also does not apply to a school referendum levy that was approved by the voters before the zone is designated.

Individual Income Tax Exemption: A subtraction from federal taxable income would be allowed to an individual who operated or invested in a trade or business located in a zone. The subtraction would apply to net income from operating a business in a zone, net rental income derived from real or personal property in a zone, and net capital gains related to zone investment. A similar subtraction would be allowed in computing alternative minimum taxable income.

Corporate Franchise Tax Exemption: A subtraction from taxable income would be allowed for income derived from the operation of a business in the biotechnology zone. A subtraction would also be allowed in computing alternative minimum taxable income and the property and payroll factors for the minimum fee.

Sales Tax Exemption: Purchases of tangible personal property and taxable services by a qualified business are exempt from the sales and use tax if the property and services are primarily used or consumed in a biotechnology zone. An exemption would also be allowed for construction materials and supplies for the improvement to real property in a zone used in the conduct of a qualified business, regardless of whether purchased by the business or a contractor. These transactions would also be exempt from local sales and use taxes.

Motor Vehicle Sales Tax Exemption: An exemption from motor vehicle sales tax would be allowed for the purchase of a vehicle by a person engaged in a trade or business located in the zone if the vehicle is garaged in the zone and used primarily for the business operation in the zone. These vehicles would also be exempt from local sales and use taxes.

Repayment: Section 21 provides for the repayment of tax reductions if a business relocates into a biotechnology zone and then ceases to operate the facility within the zone. A business must repay the amount of tax reduction or local contribution received during the two years immediately before it ceased to operate in the zone.

REVENUE ANALYSIS DETAIL

- The state revenue forecast is based on a forecast of all economic activity in the state, including that which may occur in a biotechnology zone. Therefore, forecasted state revenues would be reduced if one or more state tax exemptions were enacted for the zone.
- This analysis assumes that there will be two biotechnology subzones, one in Minneapolis and one in St. Paul by calendar year 2006.
- Information from the developer indicates that a 100,000 square foot building will be constructed in Minneapolis in 2004. Another similar building will be constructed in St. Paul in 2005.
- An additional 100,000 square feet of building space will be added to the Minneapolis site in 2005.
- A combined total of 200,000 square feet of building space will be added to the zone in 2006.
- Based on data from similar types of buildings, the estimated employment per 100,000 square feet building space is 100.
- Because of their specialized nature, the cost per square foot of buildings in a biotechnology zone is assumed to be \$150 and the cost per square foot of equipment is assumed to be \$150 per square foot.

Property Tax

- Information from the developer indicates that a 100,000 square foot building will be constructed in Minneapolis in 2004. The improvements will cost an estimated \$150 per square foot for the real estate portion of the project. Another similar building will be constructed in St. Paul and the Minneapolis site will be expanded in 2005. Expansion at both sites is expected in 2006.
- The Minneapolis improvements will add \$15 million in market value to the tax base for the January 2005 assessment, taxes payable in 2006.
- The proposed exemption in Minneapolis will cause a tax shift of \$546,000 to other taxpayers including homeowners, and increase homeowner property tax refunds by \$14,000 in F.Y. 2007.
- The proposed exemption in St. Paul for assessment year 2006, taxes payable in 2007 will not affect the state budget during the forecast period.
- The exemption from the state general levy would have no impact on state revenues. The tax rate would be adjusted to yield the amount of revenue required by statute.

Corporate Franchise Tax

- Based on state revenue forecast data for corporate franchise tax collections and statewide employment, a per-job tax collection amount was calculated.
- The per-job corporate franchise tax collection figure is \$256 in FY 2005, \$248 in FY 2006, and \$241 in FY 2007.
- This per-job corporate franchise tax collection number was aggregated based on biotechnology zone employment estimates.
- All business and investment income is accounted for in the corporate franchise tax estimates.

REVENUE ANALYSIS DETAIL (cont.)

Sales and Use Tax

- The revenue impact from sales tax exemptions is calculated for two categories, initial construction and ongoing purchases.
- Construction materials and initial furnishings were calculated as 45% of total building costs.
- It is not known to what extent the equipment would qualify under an existing sales tax exemption. The capital equipment exemption can include machinery and equipment used for research and development, design, and testing if it is essential to manufacturing a product to be sold ultimately at retail. In the absence of specific information, it was estimated that taxable equipment would be 45% of total equipment spending.
- An estimate for ongoing purchases, such as office furnishings, utilities, and supplies, was based on state revenue forecast data for sales tax collections and statewide employment to calculate a per-job tax collection number.
- Due to the specialized nature of materials and services purchased in the zone, the per-job sales tax is \$938 in FY 2005, \$974 in FY 2006, and \$1,007 in FY 2007.
- Combined with projected annual employment in the zone, an estimate for sales tax exemptions for ongoing purchases was calculated.

Number of Taxpayers Affected: It is expected that several businesses would eventually be located in each subzone, but the total is not known.

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