Estimates of Life Sciences Tax Incentives

Assumed to be Available to All Life Sciences Companies

(Different From Governor's Proposal, Which is Project-Specific and Subject to Annual Cap)

Effective Date: Assumed to be 1/1/2008

	Tax Incentive	Annualized Revenue Impact (Static Estimate)
1	Refundable 10% Investment Tax Credit (ITC) for Life Sciences Companies (10 to 10)	-$20.5 Million to -$24.5 Million (eliminate)
2	Additional ITC for Projects Located in Economic Opportunity Areas	-$5.5 Million to -$8.0 Million
3	Life Sciences Human Drug User Fee Credit	-$13.6 Million to -$20.4 Million
4	Net Operating Loss (NOL) Carryover for Life Sciences Companies Extended from Current 5 Years to 15 Years	Estimate not Available
5	Eliminate MA Throwback Provision for Life Sciences Companies (Cap Excise)	-$3.0 Million to -$6.0 Million
6	a) Certified projects considered Research and Development Entities for the Purposes of Sales Tax Exemptions	Estimate Not Applicable - Proposal is Integral to Certified Projects (eliminate)
	b) Refundability of Research and Development Tax Credit	Estimate Not Available
7	Sales Tax Exemption Created for the Expansion of Utility Support Systems for Life Sciences Companies	-$1.0 Million to -$6.0 Million

The Commonwealth of Massachusetts
Department of Revenue
Office of the Commissioner
P.O. Box 9550
Boston, MA 02114-9550

HENRY DORMITZER
COMMISSIONER

January 29, 2008

The Honorable Robert A. DeLeo
Chairman
House Committee on Ways and Means
State House, Room 243
Boston, MA 02133 - 1054

Dear Chairman DeLeo:

This letter is in response to your request, dated January 17, 2008, that the Department of Revenue provide additional information to that contained in an analysis sent to the Joint Committee on Economic Development and Emerging Technologies on October 29, 2007. In that letter the Department provided estimates of the Governor's proposal, (H.4234, "An Act Providing For Investment in and Expansion of the Life Sciences Industry in the Commonwealth"). In estimating the impact of H.4234, the Department's October 29th response assumed that the Administration, as it has publicly stated, would impose a $25 million annual cap on tax benefits. The Department also estimated that there would be a large enough supply of certified life sciences projects to reach the $25 million cap each year, and that because particular tax incentives would be provided at the discretion of the Secretaries of Housing and Economic Development and Administration and Finance, for the Governor's proposal it is not possible to predict the value of a particular tax incentive for a particular year.

In addition to providing estimates for H.4234 as filed, the October 29th letter responded to the Joint Committee's request that the Department provide revenue impact estimates for the tax incentives proposed in H.4234, under the assumption that there would not be a $25 million annual cap imposed on tax benefits, i.e., that all life sciences companies would be eligible for the tax benefits without restriction. The Department was able to provide estimates for five of the seven proposals, and stated that it did not have the data available to estimate the impact of extending the net operating loss claim period from 5 to 15 years or making the research and development credit refundable. We also noted that in order to estimate the impact of granting all life sciences companies Research and Development status (which would make them eligible for sales tax exemptions), we would need further guidance as to the criteria that should be used to determine whether a corporation is eligible for Research and Development status.

Your January 17th letter made two requests: (1) That the Department provide revenue estimates for the net operating loss, research and development status, and refundable research credit proposals that we were unable to provide in our October 29th letter; and (2) that the Department provide a more detailed explanation of the methodology for the five estimates that were provided in the October 29th letter. In the interest of expediting our response, this letter responds to question (1), the revenue estimates for those proposals which we were

unable to provide in the October 29th letter. Within the next few days, we will also send to you a more detailed explanation of how we arrived at the five revenue estimates that we did include in the October 29th letter.

Methodology. For each of the estimates below, we extracted the relevant tax information from Massachusetts corporate excise returns. In determining which corporations were in the "life sciences" industry, we used the definition from the Massachusetts Technology Collaborative's April 2007 report, *SuperCluster: Ideas, Perspectives and Updates from the Massachusetts Life Sciences Industry*. As such, the life sciences industry includes the following industry subsectors:

Industry Name	NAICS (Industry) Code*
Pharmaceutical & Medicine Manufacturing	325410-414
Medical Devices and Equipment: Navigational, Measuring, Electromedical, and control instruments	334500
Medical Devices and Equipment: Navigational, Measuring, Electromedical, and Control instruments: Analytical Laboratory Instrument Manufacturing	334516
Medical Equipment & Supplies Manufacturing	339110
Wholesale Trade: Medical, Dental, & Hospital Equipment & Supplies Merchant wholesalers or Ophthalmic Goods Merchant Wholesalers	423400
Wholesale Trade: Drugs & Druggists' Sundries Merchant Wholesalers	424210
Medical and Testing Laboratories: Testing Laboratories	541380
Biotechology: Scientific Research & Development Services	541700
Medical and Testing Laboratories	621510

* Includes other six digit NAICS codes within these categories

It should be noted that these definitions are to some extent arbitrary, and any narrowing or expanding of the definitions would reduce or increase the revenue impact estimates provided herein.

The number of corporations filing tax returns in the life sciences industry as defined above has increased substantially in recent years. In tax year 1999, the number of corporate filers in the life sciences industry was approximately 1,769; in tax year 2005 (the most recent year for which data are available), the number of corporate filers in the life sciences industry was approximately 2,577, an increase of approximately 46% from 1999.

Revenue Estimates

Net Operating Loss (NOL) Carryover for Certified Life Sciences Projects Extended from the Current 5 Years to 15 Years.

The Department captures tax return data on the amount of net operating loss carryovers used in a particular tax year, but does not capture data on the amount of unused carryovers or the amount of carryovers that have expired due to the current 5 year limitation. In order to estimate the unused net operating loss carryovers, we examined the amount of losses generated by loss-making corporations in the life sciences industry, and attempted to reconstruct the historical pattern of the use of net operating losses. We assumed that the extension in the NOL carryover period from 5 to 15 years would apply only to losses generated starting in tax year 2008, and would not apply to accumulated carryovers generated through tax year 2007. Consequently, there would be no revenue impact for tax years 2008 through 2012, since net operating losses generated in those years would be useable under the current 5 year limitation, so would not be affected by the extension in the carryover period to 15 years. Only in tax year 2013, when some of those losses would expire under the current 5 year limitation, would an extension to a 15 year period result in revenue reductions relative to current law. There would also be a lag in the fiscal year impact; since fiscal year 2013 begins midway through tax year 2012, the full impact of a revenue reduction in tax year 2013 would not be felt until fiscal year 2014.

If the carryover extension is applied to net operating losses generated through tax year 2007, the revenue loss would be greater than shown below, and would begin to be felt in the first tax and fiscal year in which the legislation was enacted.

The magnitude of operating losses is large in the life sciences industry, much larger than the amount of net operating losses used in any particular year. According to tax return data, over the tax year 2000 to 2005 period, net operating losses for life sciences corporations averaged approximately $2.1 billion after apportionment (approximately $200 million after applying the 9.5% corporate tax rate), while net operating loss carryovers used by life sciences corporations averaged about $314 million (approximately $30 million at the 9.5% corporate tax rate). As noted above, the Department does not have data on how much in net operating loss carryovers expired due to the 5 year limitation (or how many of these carryovers were unused because a company went out of business due to persistent losses), but given the large and persistent discrepancy between the amount of losses generated and losses used (about $170 million annually), it is highly likely that a large, though indeterminate amount of net operating losses could be used by life sciences corporations that eventually become profitable if the carryover period were extended from 5 to 15 years. Assuming 5% to 10% annual growth in both net operating losses and the use of net operating loss carryovers by life sciences corporations, and that between 20% and 50% of the annual average difference between the net operating losses and NOL carryovers used would be made usable by extending the carryover period from 5 to 15 years, the revenue loss is shown in the table below.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008-12	$0	$0	$0	$0	$0	$0.0
2013	$50	$116	$182	$30	$70	$109
2014	$53	$127	$200	$50	$116	$182

Given the fact that this change would not affect state revenues until tax year 2013, the absolute magnitude of the revenue loss estimate should be considered highly uncertain. However, given the size of the annual losses generated by the life sciences industry, and the relatively small amount of carryover losses utilized annually, we believe that the potential revenue loss from extending the net operating loss carryover period from 5 to 15 years would be at least in the tens of millions of dollars.

Refundable Research Tax Credit

Under current law, research credits may be claimed by corporations that have incurred basic research payments and/or qualified research expenses for research conducted in Massachusetts, subject to certain limitations. The credits are not refundable and can be carried forward to future years. Under the Governor's proposal, "life sciences" industry filers would be able to receive refundable credits, (i.e., they would receive refunds if their tax liability is less than the amount of the research credit for which they are eligible), to the extent that the credit is more than the corporation's tax liability. In order to estimate the impact of this proposal, the Department extracted data from tax returns for all companies falling into the life sciences NAICS code categories. In tax year 2005, the amount of research credits generated by life sciences corporations totaled approximately $93 million, while the amount of credits actually utilized by life sciences corporations totaled approximately $27 million. Thus, had refundable research tax credits been in place for tax year 2005 for the life sciences industry, the additional revenue loss to the Commonwealth would have been approximately $66 million ($93 million minus $27 million). As of tax year 2005, approximately $270 million in life sciences industry research credits had been carried over from prior years (including the $93 million generated in tax year 2005).

Given the continuing growth in the life sciences industry, it is likely that research spending (and thus research credits) by the life sciences industry will increase over the near term. For the purpose of this estimate, we have assumed a growth rate of between 5% annually (for the lower bound estimate) and 10% annually (for the upper bound estimate). We also assumed a 1 year lag between the tax year and fiscal year impact, as corporations would not be able to claim their refundable credits until tax returns are filed after the end of the tax year.

As this estimate is based upon tax return information, we are reasonably certain of its accuracy. However, it should be noted that we have not explicitly adjusted the estimate for the potential incentive effect of a

refundable credit. This could increase the amount of research investment, and thus also increase the revenue loss beyond what is estimated below.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$76.4	$82.1	$87.8	$0.0	$0.0	$0.0
2009	$80.2	$88.4	$96.6	$76.4	$82.1	$87.8
2010	$84.2	$95.3	$106.3	$80.2	$88.4	$96.6

Research and Development Status for Life Sciences Companies (Sales Tax Exemption)

Under current law, to qualify for a sales tax exemption a corporation must either be a domestic or foreign manufacturing corporation or a "research and development" corporation. To be a research and development corporation, a company must satisfy the following conditions:

- the corporation must be engaged in research and development in Massachusetts;
- its principal activity in Massachusetts must be research and development;
- during the taxable year, one of the following tests must be met:
  - the corporation must derive more than 2/3 of its receipts attributable to Massachusetts from research and development; or
  - it must incur more than 2/3 of its expenditures attributable to Massachusetts for research and development.

Currently, all corporations, including those in the life sciences industry, are eligible for research and development status if they satisfy the conditions set out above. As the Department pointed out in its October 29th letter, absent the project certification provisions of the Governor's proposal, there would need to be further specification of the conditions under which a corporation would qualify for research and development status in order for the Department to estimate a revenue impact of the law change. For the purpose of this estimate, we have assumed that in addition to research and development status, a new "life sciences" status would be created for corporations in the life sciences industry. All corporations in that industry would receive a sales tax exemption for the same types of research and development purchases that are currently exempt for research and development corporations.

Based on this assumption, the Department tabulated research expense data from the tax returns of all corporations with life science industry NAICS codes, but which are not currently classified as either manufacturing or research and development corporations. For tax year 2005, research expenses for these life sciences corporations totaled $371 million. The proportion of research expenditures subject to the sales tax

varies from company to company, but based on a sample of tax returns (which include information that can be used to estimate the proportion of research expenses that is subject to sales tax), we estimate that the proportion of research and development expenses subject to the sales tax ranges from 20% to 50%. Applying this percentage range to the $371 million research expenditure base, and also applying a 5% sales tax rate, yields a sales tax revenue amount of $3.7 million to $9.3 million for tax year 2005, which would be the amount that would have been foregone if these corporations had been exempted from the sales tax on these expenditures. Applying a growth rate between tax year 2005 and tax year 2008 yields a 2008 revenue loss estimate of $5 million to $13 million. We have assumed an effective date of March 1, 2008 (2/3 of the way through fiscal year 2008), and no growth in the years after 2008 due to the current uncertainty regarding the economic outlook for those years.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$5.0	$9.0	$13.0	$1.7	$3.0	$4.3
2009	$5.0	$9.0	$13.0	$5.0	$9.0	$13.0
2010	$5.0	$9.0	$13.0	$5.0	$9.0	$13.0

As it is based on expenditure data from Massachusetts corporate tax returns, we are reasonably certain of the sales tax exemption estimate.

Please do not hesitate to contact me or my staff directly if you have additional questions about this analysis.

Sincerely,

Navjeet K. Bal

Navjeet K. Bal
Senior Deputy Commissioner

CC: The Honorable Steven C. Panagiotakos, Chairman, Senate Committee on Ways and Means
The Honorable Daniel E. Bosley, House Chairman, Joint Committee on Economic Development and Emerging Technologies
The Honorable John A. Hart, Jr., Senate Chairman, Joint Committee on Economic Development and Emerging Technologies
The Honorable John J. Binienda, House Chairman, Joint Committee on Revenue
The Honorable Cynthia Stone Creem, Senate Chairwoman, Joint Committee on Revenue
Leslie A. Kirwan, Secretary, Executive Office of Administration and Finance
Daniel O'Connell, Secretary, Executive Office of Housing and Economic Development

HENRY DORMITZER
COMMISSIONER

The Commonwealth of Massachusetts
Department of Revenue
Office of the Commissioner
P.O. Box 9550
Boston, MA 02114-9550

February 1, 2008

The Honorable Robert A. DeLeo
Chairman
House Committee on Ways and Means
State House, Room 243
Boston, MA 02133 - 1054

Dear Chairman DeLeo:

This letter represents the second and final component of the Department of Revenue's response to your request, dated January 17, 2008, that DOR provide additional information with respect to an analysis sent to the Joint Committee on Economic Development and Emerging Technologies on October 29, 2007. Your January 17th letter made two requests: (1) that the Department provide revenue estimates for the proposals relating to net operating losses, research and development status, and refundable research credits that we were unable to provide in our October 29th letter; and (2) that the Department provide a more detailed explanation of the methodology for the five estimates that were provided in the October 29th letter. Our January 29, 2008 letter to you addressed your first request; this letter completes our response, providing a more detailed explanation of the five estimates included in the October 29th letter. Please note that in the case of the refundable investment tax credit and sales tax exemption estimates, we have updated our analysis to incorporate final tax year 2004 tax return information and preliminary tax year 2005 data. (This resulted in higher estimates for those two items.) Our October 29th analysis was based on preliminary tax year 2004 information.

Please also note that the summaries and estimates contained herein assume that there would not be a $25 million annual cap imposed on tax benefits (i.e., that all life sciences companies would be eligible for the tax benefits without restriction). As you know, this assumption is a deviation from Governor's proposal, H.4234, which would provide a menu of tax benefits potentially extended to certified projects and administratively impose a $25 million annual cap on the amount of such tax benefits that could be approved. (Please see the October 29th and the January 29th letters for a more detailed explanation of the Governor's proposal.)

Methodology. In generating the estimates shown below, we extracted relevant tax information from tax year 2004 and 2005 Massachusetts corporate excise returns, to the extent such information was available. In determining which corporations were in the "life sciences" industry, we used the definition from the Massachusetts Technology Collaborative's April 2007 report, *SuperCluster: Ideas, Perspectives and Updates from the Massachusetts Life Sciences Industry*. As such, the life sciences industry includes the following industry subsectors:

Industry Name	NAICS (Industry) Code*
Pharmaceutical & Medicine Manufacturing	325410-414
Medical Devices and Equipment: Navigational, Measuring, Electromedical, and control instruments	334500
Medical Devices and Equipment: Navigational, Measuring, Electromedical, and Control instruments: Analytical Laboratory Instrument Manufacturing	334516
Medical Equipment & Supplies Manufacturing	339110
Wholesale Trade: Medical, Dental, & Hospital Equipment & Supplies Merchant wholesalers or Ophthalmic Goods Merchant Wholesalers	423400
Wholesale Trade: Drugs & Druggists' Sundries Merchant Wholesalers	424210
Medical and Testing Laboratories: Testing Laboratories	541380
Biotechology: Scientific Research & Development Services	541700
Medical and Testing Laboratories	621510

* Includes other six digit NAICS codes within these categories

As we noted in our January 29th letter, these definitions are to some extent arbitrary, and any narrowing or expanding of the definitions would reduce or increase the revenue impact estimates provided herein.

The number of corporations filing tax returns in the life sciences industry as defined above has increased substantially in recent years. In tax year 1999, the number of corporate filers in the life sciences industry was approximately 1,769; in tax year 2005 (the most recent year for which data are available), the number of corporate filers in the life sciences industry was approximately 2,577, an increase of approximately 46% from 1999.

Revenue Estimates

Refundable 10% Investment Incentive Tax Credit (ITC) for Life Sciences Companies. (Bill Sections 14 & 21)

The investment tax credit (ITC) is currently available to manufacturing or research and development corporations at a rate of 3% of qualified expenditures (or 5% of expenditures if they are made within certified Economic Opportunity Areas). The Life Sciences Investment Incentive Tax Credit proposal would create a 10% refundable tax credit that could be provided to any certified life sciences project (whether undertaken by an individual or corporation) equal to 10% of the cost of certain property associated with such a project. If the approved individual or corporation so chooses, it could carry over the tax credit for 10 years, instead of taking the refund in the first year. Section 14 would amend section 6 of c. 62, the personal income tax chapter; Section 21 would add a new section 38U of c. 63, the corporate excise chapter.

To estimate the "uncapped" revenue impact for this section of the proposal, we identified companies that would potentially qualify for the Life Sciences ITC by using the NAICS codes listed above, and extracted data from the 2004 and 2005 corporate tax return data sets. We calculated used and unused current year investment tax credits for these corporations under the current 3% ITC rule. We then calculated the incremental change in credits (used and unused) due to the proposed change in the ITC rate (from 3% to 10%). The resulting estimate was grown out to calendar year 2008 and converted to fiscal years.

Given the continuing growth in the life sciences industry, it is likely that investment spending by the life sciences industry (and thus investment tax credits generated by that industry) will increase over the near term. For the purpose of this estimate, we have assumed a growth rate of between 5% annually (for the lower bound estimate) and 10% annually (for the upper bound estimate). We assumed a one year lag between the tax year and fiscal year impact, which is reasonable for companies claiming refundable credits that would be generated as result of the incremental credit rate change and claimed when tax returns are filed after the end of the tax year.

As noted above, the estimate shown below is considerably higher than that provided in our October 29th letter, and the range of estimates is wider. The October 29th estimate was based on preliminary tax year 2004 corporate return data. Final 2004 and preliminary 2005 corporate tax return data indicate that investment by life sciences corporations was higher than originally estimated, and analysis of prior years' data indicates that such investment is quite variable from year to year. It should also be noted that most of the investment by life sciences corporations in any one year is attributable to a small number of large corporations, making it even more difficult to predict accurately. Consequently, we have widened the range of lower and upper bound estimated revenue loss impacts compared to our October 29th analysis. We also believe that there is considerable risk that the eventual revenue loss could be higher than shown below, but that risk is difficult to quantify because investments in the life sciences industry are episodic and often very large. For example, an investment project of the size reportedly being undertaken at Fort Devens (approximately $660 million, according to MassDevelopment), would, at a 10% rate, potentially qualify for a $66 million refundable investment tax credit. A final point is that with an increase in the tax credit rate to 10%, and an added refundability feature, the amount of life sciences industry investment might increase significantly above that which has occurred in the recent past, which would result in revenue losses higher than shown below.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$25.0	$37.5	$50.0	$0.0	$0.0	$0.0
2009	$26.3	$40.6	$55.0	$25.0	$37.5	$50.0
2010	$27.6	$44.0	$60.5	$26.3	$40.6	$55.0

Refundable 12% (10% plus additional 2%) Investment Incentive Tax Credit (ITC) for Certified Life Sciences Projects Located in Economic Opportunity Areas (Bill Sections 14 & 21

The investment tax credit is currently available to manufacturing or research and development corporations at a rate of 5% of qualified expenditures if those investments are made within certified Economic Opportunity Areas. The proposed Life Sciences Investment Incentive Tax Credit would provide a refundable tax credit for certified life sciences projects (whether undertaken by individuals or corporations) equal to 12% of the costs of certain property associated with a project located in Economic Opportunity Areas.

Under the proposal, if the approved individual or corporation so chooses, it could carry over the tax credit for 10 years, instead of taking the refund in the first year. Section 14 would amend section 6 of c. 62, the personal income tax chapter; Section 21 would add a new section 38U of c. 63, the corporate excise chapter.

To estimate the "uncapped" revenue impact for this section of the proposal, we identified life sciences industry companies (using the NAICS codes indicated above) currently claiming the Economic Opportunity Credit. From 2004 and 2005 corporate tax returns, we tabulated these companies' used and unused current year investment tax credits at the current 5% ITC rate. Then we calculated the incremental change in credits (used and unused) due to a change in ITC rate (5% to 12%). The resulting amount was grown out to a calendar year 2008 level and converted to fiscal years.

Given the continuing growth in the life sciences industry, it is likely that investment spending by the life sciences industry (and thus investment tax credits generated by that industry) will increase over the near term. For the purpose of this estimate, we have assumed a growth rate of between 5% annually (for the lower bound estimate) and 10% annually (for the upper bound estimate). We assumed a one year lag between the tax year and fiscal year impact, which is reasonable for companies claiming refundable credits that would be generated as result of the incremental credit rate change and claimed when tax returns are filed after the end of the tax year.

As this estimate is based upon tax return information, we are reasonably certain of the base amounts used to calculate it. However, as with the investment tax credit estimate above, we believe that the range of the estimate provided below should be considered a minimum, as we have not explicitly adjusted it for the potential incentive effect of an incremental ITC rate change and a refundability feature. Such changes could increase the amount of investment spending, and thus also increase the revenue loss above what is estimated below.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$5.5	$6.8	$8.0	$0.0	$0.0	$0.0
2009	$5.8	$7.3	$8.8	$5.5	$6.8	$8.0
2010	$6.1	$7.9	$9.7	$5.8	$7.3	$8.8

Certified Life Sciences Project User Fee Credit. (Bill Sections 15 & 17)

The proposed User Fee Credit would be a 100% refundable credit for human drug or supplement application fees paid by a project to the U.S. Food and Drug Administration (USFDA), for products primarily researched and developed in Massachusetts. Section 15 amends section 6 of chapter 62; section 18 amends chapter 63 by adding a new section 31M.

DOR does not have any in-house data on human drug or supplement application fees paid by Massachusetts companies to the USFDA. However, based on data from the USFDA, the amount of prescription drug user fees paid in FY07 totaled $316.7 million, an amount which grew by approximately 7.5% annually between FY05 and FY07. To estimate the "uncapped" value of this proposal, we converted the federal fiscal year amounts to calendar year amounts, and allocated these payments to Massachusetts using information on Massachusetts' share of national life sciences company payroll and the shipment value of life sciences related products[1], using a range of 4% (for the lower bound estimate) to 6% (for the upper bound estimate). For the purpose of this estimate, we have assumed a growth rate of between 5% annually (for the lower bound estimate) and 10% annually (for the upper bound estimate). We assumed a one year lag between the tax year and fiscal year impacts, which is reasonable for companies that would claim refundable credits when tax returns are filed after the end of the tax year.

As this estimate is based upon actual user fees paid to the federal government, we are reasonably certain of its accuracy. However, it should be noted that we have not explicitly adjusted the estimate for the potential incentive effect of the refundable user fee credit. This could increase the number of human drug review applications and user fee payments, and thus also increase the revenue loss above what is estimated below.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$13.6	$17.0	$20.4	$0.0	$0.0	$0.0
2009	$14.3	$18.4	$22.4	$13.6	$17.0	$20.4
2010	$15.0	$19.8	$24.7	$14.3	$18.4	$22.4

[1]Source: 2002 U.S. Economic Census

Massachusetts "Throwback Sales Provision" Eliminated For Certified Life Sciences Projects. (Bill Section 18)

Under current law, corporations subject to a so-called Massachusetts "throwback" rule who make sales to out-of-state customers are generally required to source or allocate such sales to Massachusetts in certain cases where the seller is not taxable in the customer's state. The application of the throwback rule thus increases the corporation's apportionment of income to Massachusetts, and potentially increases its tax liability. Under this proposal, which amends section 38 of chapter 63, sales by certified projects of products manufactured in Massachusetts could be "sourced" to a customer's state outside of Massachusetts.

Information on throwback sales is collected on Massachusetts corporate tax returns. To estimate the "uncapped" revenue impact of eliminating the throwback provisions for all life sciences corporations, we calculated the increase in tax liability for these corporations (using the NAICS codes indicated above) as reported on corporate tax returns. Based on these data, we calculated that the tax impact of eliminating the throwback provisions for all life sciences corporations would range from $3 million to $6 million annually.

Given the continuing growth in the life sciences industry, it is likely that such throwback sales by the life sciences industry will increase over the near term. For the purpose of this estimate, we have assumed a growth rate of between 5% annually (for the lower bound estimate) and 10% annually (for the upper bound estimate). We assumed a one year lag between the tax year and fiscal year impacts.

As this estimate is based upon tax return information, we are reasonably certain of its accuracy. However, it should be noted that we have not explicitly adjusted the estimate for the potential incentive effect of the elimination of the throwback sales provision. *Increased sales due to this incentive effect could result in* revenue losses greater than shown in the estimate below.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$3.0	$4.5	$6.0	$0.0	$0.0	$0.0
2009	$3.2	$4.9	$6.6	$3.0	$4.5	$6.0
2010	$3.3	$5.3	$7.3	$3.2	$4.9	$6.6

Sales Tax Exemption Created for the Expansion of Utility Support Systems Associated with a Certified Life Sciences Project. (Section 23)

This provision provides that utility support system costs associated with a certified life sciences project be exempted from the state sales tax. Section 23 amends section 6 of chapter 64H. The sales tax exemption would apply to tangible personal property purchased for a certified life sciences project, as defined by section 63 of chapter 23A, for use in connection with the construction, alteration, remodeling, repair, or remediation of research, development or manufacturing facilities and utility support systems, in furtherance of a certified life sciences project.

The Department does not have good data with which to estimate the amount of spending on such projects that is currently subject to the sales tax. To estimate the "uncapped" revenue impact of this provision, we assumed that total spending on such projects would be identical to spending eligible for the investment tax credit estimated above. We also assumed that the proportion of such costs that would be subject to the sales tax under current law (and which would be exempt from sales tax under this proposal) would range from 5% (for the lower bound estimate) to 30% (for the upper bound estimate) of total investment spending. Using these assumptions, we estimated that this provision would result in a tax revenue loss of between $2 million and $10 million annually. Because this estimate is based on the investment tax credit data, it is also higher than originally shown in our October 29th letter.

We have assumed an effective date of March 1, 2008 for the life sciences legislation, so there would be a part-year revenue impact in FY08 and a full-year revenue impact beginning in FY09.

In addition to the uncertainty surrounding the investment data upon which this estimate is based, there is also significant uncertainty regarding the proportion of those expenditures that are currently subject to the sales tax. Consequently, we have provided a wide range for the lower and upper bounds of the estimate.

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$2.0	$6.0	$10.0	$0.5	$1.5	$3.3
2009	$2.1	$6.6	$11.0	$2.1	$6.3	$10.5
2010	$2.2	$7.2	$12.1	$2.2	$6.9	$11.6

We trust that this letter completes the Department's response to your request dated January 17, 2008. Please do not hesitate to contact me or my staff directly if you have additional questions about this response or our previous analyses.

Sincerely,

Navjeet K. Bal

Navjeet K. Bal
Senior Deputy Commissioner

CC: The Honorable Steven C. Panagiotakos, Chairman, Senate Committee on Ways and Means
The Honorable Daniel E. Bosley, House Chairman, Joint Committee on Economic Development and Emerging Technologies
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Office of the Commissioner
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NAVJEET K. BAL
COMMISSIONER

February 7, 2008

Amend it 70% business in mass get SSF

The Honorable Daniel E. Bosley
House Chairman
Joint Committee on Economic Development and Emerging Technologies
State House, Room 42
Boston, MA 02133 - 1020

Dear Chairman Bosley:

The Department is responding to your question, relayed to DOR by Maureen Flynn of the Executive Office of Housing and Economic Development, regarding the cost of extending the use of single sales factor apportionment to certain companies in the "life sciences" industry that do not currently qualify for this apportionment method. (Under current law, single sales factor apportionment is limited to manufacturing corporations, which may or may not be life sciences companies, and to mutual fund services corporations.)

Given the Commonwealth's experience with single sales factor apportionment and single entity reporting to date, the Secretary of Administration and Finance and the Department strongly recommend that any extension of single sales factor apportionment to life sciences companies be mandatory, not elective, and be adopted in conjunction with combined reporting and mandatory check-the-box entity classification to minimize the opportunities for companies to arrange their corporate structure so as to avoid taxation in Massachusetts. In addition, to avoid a challenge under the U.S. Constitution's Commerce Clause, the Department recommends that any extension of single sales factor apportionment to the life sciences industry should be to all life sciences companies, and not just those that have a certain percentage of payroll or property in Massachusetts.

In order to be as responsive as possible to your inquiry, we are providing revenue loss estimates for both the impact of single sales factor apportionment for life sciences companies with at least 70% of their payroll or property apportioned to Massachusetts, and the impact of single sales factor apportionment for all life sciences companies which are currently subject to tax in Massachusetts. We will assume that if implemented, the single sales factor apportionment would be mandatory for the specified life science companies, which is consistent with the existing mandatory single sales factor methodology for manufacturers and mutual fund service corporations. An elective single sales factor methodology would have a higher revenue cost than what is estimated below.

In generating the estimates shown below, we extracted relevant tax information from tax year 2004 and 2005 Massachusetts corporate excise returns, to the extent such information was available. In determining which corporations were in the "life sciences" industry, we used the definition from the Massachusetts Technology Collaborative's April 2007 report, *SuperCluster: Ideas, Perspectives and Updates from the Massachusetts Life Sciences Industry*. As such, the life sciences industry includes the following industry subsectors:

Industry Name	NAICS (Industry) Code*
Pharmaceutical & Medicine Manufacturing	325410-414
Medical Devices and Equipment: Navigational, Measuring, Electromedical, and control instruments	334500
Medical Devices and Equipment: Navigational, Measuring, Electromedical, and Control instruments: Analytical Laboratory Instrument Manufacturing	334516
Medical Equipment & Supplies Manufacturing	339110
Wholesale Trade: Medical, Dental, & Hospital Equipment & Supplies Merchant wholesalers or Ophthalmic Goods Merchant Wholesalers	423400
Wholesale Trade: Drugs & Druggists' Sundries Merchant Wholesalers	424210
Medical and Testing Laboratories: Testing Laboratories	541380
Biotechology: Scientific Research & Development Services	541700
Medical and Testing Laboratories	621510

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The proposed legislation specifies that single sales factor apportionment would apply to life sciences companies that have either 70% of certain categories of employees based in Massachusetts or 70% of property located in Massachusetts. However, Massachusetts corporate tax returns do not contain information on the number of employees a corporation has in Massachusetts compared to the total number of employees for that corporation. Massachusetts corporate tax returns do provide information on the amount of payroll a corporation attributes to Massachusetts as a proportion of total payroll for that corporation, and we have used that information as an approximation for the employment provisions of the proposed legislation. Based on our analysis of tax return data, approximately 39 life sciences corporations that used three-factor apportionment in tax year 2005 would have been eligible for single sales factor apportionment under the proposed legislation, which would have resulted in a revenue loss of approximately $3.2 million. Using an appropriate growth factor from tax years 2005 to 2008, the tax year 2008 revenue loss from utilizing single sales factor apportionment would have been **$4.4** million.

Had single sales factor apportionment been available to all life sciences corporations, and not just those that met the 70% payroll or property requirements, approximately 335 life sciences corporations that used three-factor apportionment in tax year 2005 would have been eligible for single sales factor apportionment, which would have resulted in a revenue loss of approximately $16.2 million. Using an appropriate growth factor from tax years 2005 to 2008, the tax year 2008 amount is estimated to be **$21.9** million.

Given the continuing growth in the life sciences industry, it is likely that profits (and taxable income) of life sciences corporations will increase over the near term. For the purpose of this estimate, we have assumed a growth rate of between 5% annually (for the lower bound estimate) and 10% annually (for the upper bound estimate) for years after 2008. We assume a March 1, 2008 enactment date for the life sciences legislation, but with an effective date of January 1, 2008, too late to have an impact on estimated tax payments in FY2008. However, the FY2009 revenue impact would include both the full tax year 2008 revenue loss and a revenue

reduction in corporate estimated payments in the first half of tax year 2009. The FY2010 impact would then revert to roughly a full year tax revenue loss (the second half of tax year 2009 and the first half of tax year 2010).

Revenue Loss Resulting from Mandatory Single Sales Factor Apportionment for Life Sciences Corporations with 70% of Payroll or Property Located in Massachusetts

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$3.5	$4.4	$5.3	$0.0	$0.0	$0.0
2009	$3.7	$4.8	$5.8	$5.7	$7.3	$8.8
2010	$3.9	$5.1	$6.4	$3.8	$5.0	$6.2

Revenue Loss Resulting from Mandatory Single Sales Factor Apportionment for All Life Sciences Corporations

	Static Tax Year Impact (in $ millions)			Static Fiscal Year Impact (in $ millions)		
	Lower Bound	Midpoint	Upper Bound	Lower Bound	Midpoint	Upper Bound
2008	$17.5	$21.9	$26.3	$0.0	$0.0	$0.0
2009	$18.4	$23.7	$28.9	$28.6	$36.1	$43.6
2010	$19.3	$25.6	$31.8	$18.8	$24.4	$30.1

The above calculations assume that manufacturing corporations would be required to use single sales factor apportionment, as they are under current law. It should be noted, however, that had *optional* single sales factor apportionment been available to manufacturing life sciences corporations in tax year 2005, it would have been beneficial for 59 of the 197 life sciences corporations that used single sales factor apportionment to have switched to three factor apportionment, with a resulting additional revenue loss of $7.9 million. Using an appropriate growth factor from tax years 2005 to 2008, the tax year 2008 revenue loss from such optional treatment is estimated to be $10.6 million.

As the above estimates are based upon tax return information, we are reasonably certain of their accuracy. However, it should be noted that we have not explicitly adjusted the estimate for the potential incentive effect

of single sales treatment for life sciences companies. Increased economic activity by life sciences corporations due to this incentive effect could result in static revenue losses greater than shown in the estimates above.

If you have any questions concerning these estimates, please contact me (at 617-626-2201), or Howard Merkowitz, Director of the Office of Tax Policy Analysis (at 617-626-2100).

Sincerely,

Navjeet K. Bal

Navjeet K. Bal
Commissioner

Attachment

CC:

The Honorable John A. Hart, Jr., Senate Chairman, Joint Committee on Economic Development and Emerging Technologies
The Honorable Robert A. DeLeo, Chairman, House Committee on Ways and Means
The Honorable Steven C. Panagiotakos, Chairman, Senate Committee on Ways and Means
The Honorable John J. Binienda, House Chairman, Joint Committee on Revenue
The Honorable Cynthia Stone Creem, Senate Chairwoman, Joint Committee on Revenue
Leslie A. Kirwan, Secretary, Executive Office of Administration and Finance
Daniel O'Connell, Secretary, Executive Office of Housing and Economic Development
Maureen Flynn, Executive Office of Housing and Economic Development
Robert Brandt, Joint Committee on Economic Development and Emerging Technologies

Massachusetts Life Sciences Initiative
Tax Provisions

Proposed Amendment: Page 6, Section 7. New. Insert after line 38. "Qualified US Life Science Headquarters", an affiliated group, as defined in Section 1504(a) of the Internal Revenue Code of 1986 that derives at least 70 percent of its revenue from the sale or license of life science products or intellectual property, or the rendering of contract life sciences services, or the combination of the two, if either (1) greater than 70 percent of all commercial employees, excluding sales representatives, are Massachusetts based employees, or (2) if greater than 70 percent of all tangible property (excluding inventory), leased or owned, would be apportionable to Massachusetts in the fiscal year, not withstanding the company's ability to qualify for single sales factor apportionment.

Page 24. Insert after Line 18. New. SECTION 24. Section 38 of chapter 63 of the General Laws is hereby amended by adding after subsection (n) the following subsection:-

A qualified US Life Science Headquarters Company shall be eligible to use singles sales factor apportionment for any tax year ending after enactment.

SECTION 25. Section 38(c) of chapter 63 of the General Laws is hereby amended by inserting after "a manufacturing corporation as described in subsection (l)," the following phrase:

...a qualified US Life Science Headquarters Company, as described in chapter 23A of the General Laws, Section 63(a),

Mass. Dept. of Revenue
October 19, 2007

Tax Incentives in Governor Patrick's Life Sciences Legislative Proposal

On July 19, Governor Patrick filed a legislative proposal to encourage investment in and expansion of the life sciences industry in Massachusetts. The proposed legislation, assigned docket number H 4234, would provide bond funding for capital projects and funds for fellowships, research grants and loans, and workforce training programs. In addition, the proposal would provide for certified life sciences projects and would award tax incentives to Massachusetts businesses engaged in life sciences.

Of the seven tax incentives in the proposal, three are tax credits, available to both individuals and corporations, and four are tax benefits that take other forms. The Secretary of Housing and Economic Development may award certification to an applicant life sciences sector business that is located in the Commonwealth and engaged in research, development or manufacturing. To be certified as a "certified life sciences project," a business must be engaged in the life sciences, engaged in research, development or manufacturing, and develop a new or expanded facility in the commonwealth, thereby increasing the number of its permanent full-time employees. The project's certification may be revoked if the business does not meet at least 70% of its employment goals as outlined in its proposal. The tax benefits may be awarded in some combination, on a project by project basis and to the extent provided, by the Secretary of Housing and Economic Development and the Secretary of Administration and Finance, acting jointly. The tax incentives are summarized below.

1. Life Sciences Investment Incentive Tax Credit. (Bill Sections 14 & 21)

The Life Sciences Investment Incentive Tax Credit is a 10% refundable tax credit that may be given to any certified life sciences project (individual or corporation) for 10% of the costs of certain property associated with a project. If the project so chooses, it may carry over the tax credit for 10 years, instead of taking the refund in the first year. Section 14 would amend section 6 of c. 62, the personal income tax chapter; Section 21 would add a new section 38U of c. 63, the corporate excise chapter.

2. Additional Credit for Projects Located in Economic Opportunity Areas. (Bill Sections 14 & 21)

In addition to establishing the Life Sciences Investment Tax Credit, sections 14 & 21 allow a certified project to be eligible for an additional 2% tax credit for projects located in Economic Opportunity Areas, as defined in subsection (g) of section 31A of chapter 63.

3. Certified Life Sciences Project User Fee Credit. (Bill Sections 15 & 17)

The proposed User Fee Credit is a 100% refundable credit against the fees paid by a project for application to the USFDA for a human drug application or supplement which was primarily researched and developed in Massachusetts. Section 15 amends section 6 of chapter 62; section 18 amends chapter 63 by adding a new section 31M.

4. Net Operating Loss (NOL) Carryover for Certified Life Sciences Projects Extended from the Current 5 Years to 15 Years. (Bill Section 16)

Currently, all corporations are allowed to carry over NOL deductions for 5 years. If a certified life sciences project experiences losses over a longer period of time than 5 years, the project may carry over those losses for up to 15 years. Section 16 amends section 30 of chapter 63.

5. Massachusetts "Throwback Sales Provision" Eliminated For Certified Life Sciences Projects. (Bill Section 18)

For purposes of apportionment of corporation excise tax, sales by certified projects of products manufactured in Massachusetts may be "sourced" to a customer's state outside of Massachusetts without being subject to the "throwback" rule in chapter 63 that generally requires sourcing of sales to Massachusetts in certain cases where the seller is not taxable in the customer's state. Section 18 amends section 38 of chapter 63.

6. Certified Projects Considered Research and Development Entities for the Purposes of Sales Tax Exemptions; R&D Credits May Be Refundable (Bill Sections 19 & 22; section 20)

Certified projects will be deemed to be research and development corporations, to the extent provided in the certification, without having to meet the proof requirements of that classification, in order to be exempt from the sales tax. Section 19 creates the exemption for domestic corporations and section 20 creates the exemption for foreign corporations. In addition, section 20 provides that the current research and development tax credit may be refundable for certified life sciences projects.

7. Sales Tax Exemption Created for the Expansion of Utility Support Systems Associated with a Certified Life Sciences Project. (Section 23)

This provision provides that utility support system costs associated with a certified life sciences project may be exempted from the state sales tax. Section 23 amends section 6 of chapter 64H.

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Life Sciences Initiatives:

Concerns:

- No annual cap in the legislation.
- $25M cap, stated by the administration
- Projects are chosen on criteria and projects receive funding based on the boards decision, then are given tax incentives based on the boards decision. This is arbitrary and could potentially lead to law suit down the line.
- Certified projects do not pay sales tax sales & pay roll& net worth sales factor is determined by mass sales
- The LSI eliminates the Throw back provision (out of state sales to no where brings the sales back to MA)

Thing to consider:

- Orphan Drug Credit (SERENO discussed this with us)
- Add a statutory cap on the amount of money for the LS credits
- PASS the NOL to 10 or 15 years (Chairmen Bosely and Rodrigues support this measure)
- Do not eliminate the throw back provision in the LIS
- Set qualifying standers and credit credits for those who qualify
- Single Sales Factor Amendment proposed by CM Bosely- 70% of employee base in MA or Property in MA% SSF apportionment – DOR recommends that this be mandatory not elective.

QUANTITATIVE ECONOMICS
& STATISTICS

The Economic and Fiscal Effects of Single Sales Factor Apportionment for Massachusetts Manufacturers

Prepared for the AIM Foundation

May 14, 2003

ERNST & YOUNG

Quality In Everything We Do

AIM FOUNDATION

ASSOCIATED INDUSTRIES OF MASSACHUSETTS FOUNDATION, INC.

The Associated Industries of Massachusetts Foundation, Inc., is an educational and economic research organization established by Associated Industries of Massachusetts, the largest nonprofit, nonpartisan organization of employers in the Commonwealth.

The Foundation was created in 1991 to develop in-depth, nonpartisan, fact-based analysis of public policy issues. The Foundation is classified as a Section 501(c)(3) organization under the Internal Revenue Code.

The work of the Foundation is not and should not be construed as an attempt to aid or hinder the passage of any specific legislation before the Congress or the Massachusetts Legislature.

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The Economic and Fiscal Effects of Single Sales Factor Apportionment for Massachusetts Manufacturers

Executive Summary

In determining Massachusetts corporate excise (income) tax liabilities, multi-state corporations must determine what percentage of their taxable income is attributable to their operations in Massachusetts. An apportionment formula is used to determine this percentage. In 1995, the Massachusetts legislature eliminated the payroll and property factors from the apportionment formula used by manufacturers in determining income subject to the Massachusetts corporate excise tax. This policy response was designed to slow the long-run decline in manufacturing employment and investment in Massachusetts. Compared to the double-weighted sales three-factor formula in use through 1995, the sales-only apportionment formula provides corporations with an incentive to increase payroll and property in the state. Because new in-state investments and employment do not increase a corporation's income subject to Massachusetts tax under the sales-only formula, it provides corporations with an incentive to increase their manufacturing activities in the Commonwealth.

This study provides estimates of the significant contribution the sales-only apportionment formula for manufacturers makes to Massachusetts employment, income, and state and local taxes. To measure this contribution, this study estimates the additional Massachusetts private-sector jobs, income, and state and local government taxes that the sales-only apportionment formula generates relative to the impacts of the prior-law double-weighted three-factor formula. These benefits in terms of additional jobs, income and taxes would be lost over time if Massachusetts were to return to the double-weighted sales-factor formula for manufacturers.

Key Findings

- Nearly 6,200 jobs would be lost by reverting to a double-weighted three-factor apportionment formula. The majority of these jobs are highly-skilled jobs in the durable and non-durable manufacturing sectors, which pay almost 40 percent more than the statewide average level of wages and fringe benefits.
- Although many states have increased the weight of sales factor in their corporate income apportionment formulas, this trend is especially evident among the top 10 manufacturing states. Five of the top 10 manufacturing states have adopted apportionment formulas that use sales as the sole or dominant factor.
- The sales-only apportionment formula is an efficient tax incentive. Massachusetts gains over $7.00 of additional net personal income for each dollar of reduced state corporate excise tax revenues. This is a significant long-run return in terms of new jobs and higher incomes as a result of the state's investment. In the aggregate, this manufacturing activity results in $372 million in state total personal income.
- If a double-weighted sales 3-factor apportionment formula were adopted, $52.5 million in increased excise taxes on in-state manufacturers would be largely offset by tax losses of $29.1 million in due to reduced economic activity.
- The overall budgetary impact, however, would also include additional Commonwealth spending on unemployment claims and welfare payments ($9.9 million) and potential increased transfers to local governments to compensate for a reduction in local tax revenues of ($12.2 million).
- On balance, state and local governments currently gain $41.3 million of additional tax revenue directly from the manufacturing activity attributed to the sales-only apportionment formula, which offset more than three-quarters of the static state revenue cost of the formula's cost in 2003. Projected reductions in the excise tax liabilities of out-of-state manufacturers due to double-weighted sales apportionment eliminate any remaining revenue benefit.

The Economic and Fiscal Effects of Single Sales Factor Apportionment for Massachusetts Manufacturers

I. Overview

In determining Massachusetts corporate excise tax liabilities, multi-state corporations must determine what percentage of their taxable income is attributable to their operations in Massachusetts. An apportionment formula is used to determine this percentage. For "section 38" [1] manufacturers, the percentage of profits apportioned to Massachusetts is equal to the ratio of the corporation's Massachusetts sales to its sales everywhere. This is referred to as a single (or 100 percent) sales factor apportionment formula.[2]

With the exception of mutual fund service corporations, other Massachusetts corporate taxpayers use a double-weighted sales three-factor apportionment formula. The double-weighted sales three-factor formula includes Massachusetts' shares of the corporation's payroll, property, and sales with a 50 percent weight on sales and 25 percent weights on both payroll and property factors.

The manufacturer's single sales factor apportionment formula was adopted by the state legislature in 1995 and phased in for non-defense corporations over a five-year period beginning in 1996. Tax year 2000 was the first year of the 100 percent sales factor formula for non-defense manufacturers.

The state legislature adopted the single sales factor formula to slow the long-run decline in manufacturing employment and investment in Massachusetts. Because the sales-only apportionment formula excludes payroll and property, a manufacturer may make new in-state investments and expand in-state employment without exposing itself to increased tax liability in Massachusetts. This provides the corporation with an incentive to increase its manufacturing activities in the state. In general, the change from the double-weighted sales factor formula to the sales-only formula decreases the excise tax liabilities of multi-state taxpayers with significant in-state investments and employment relative to in-state sales. Tax liabilities increased for corporations with little in-state property and payroll relative to in-state sales, primarily out-of-state corporations.[3]

This study examines the significant contribution the manufacturing single sales factor formula makes to Massachusetts employment, income, and economic activity. In addition, the study provides comprehensive estimates of the negative economic and fiscal impacts of reverting to a double-weighted sales factor formula, considering:

- Increases in excise tax collections resulting from the change in the apportionment factors used by taxpayers,
- Reductions in other state and local tax collections due to decreased economic activity attributable to the formula change, and
- Increases in public sector unemployment insurance and welfare costs associated with displaced workers.

[1] See Appendix A for the definition of a "Section 38 Manufacturer."

[2] See Appendix A for a detailed description of the Massachusetts single sales factor apportionment provisions. For purposes of this paper, the term "manufacturer" refers to manufacturers and defense contractors that qualify for single factor apportionment. While defense contractors were eligible to use the single sales factor in 1995 and while mutual fund corporations also required to use the single sales factor formula, they are not included in this study.

[3] Corporations with all of their payroll, property, and sales in Massachusetts were not affected by the change in the apportionment formula.

Apportionment Formula Trends in Other States

The clear trend since the mid-1990s has been for states to increase the weight of the sales factor beyond 50 percent. Massachusetts joins Maryland, Connecticut, Illinois, Iowa, Missouri, Nebraska, and Texas in providing manufacturers with a 100 percent sales factor apportionment formula. As shown in Table 1 and Figure 1, five additional states use sales factor weights that *exceed* 50 percent, including Michigan (90%), Oregon (80%), Minnesota (75%), Pennsylvania (60%), and Ohio (60%).

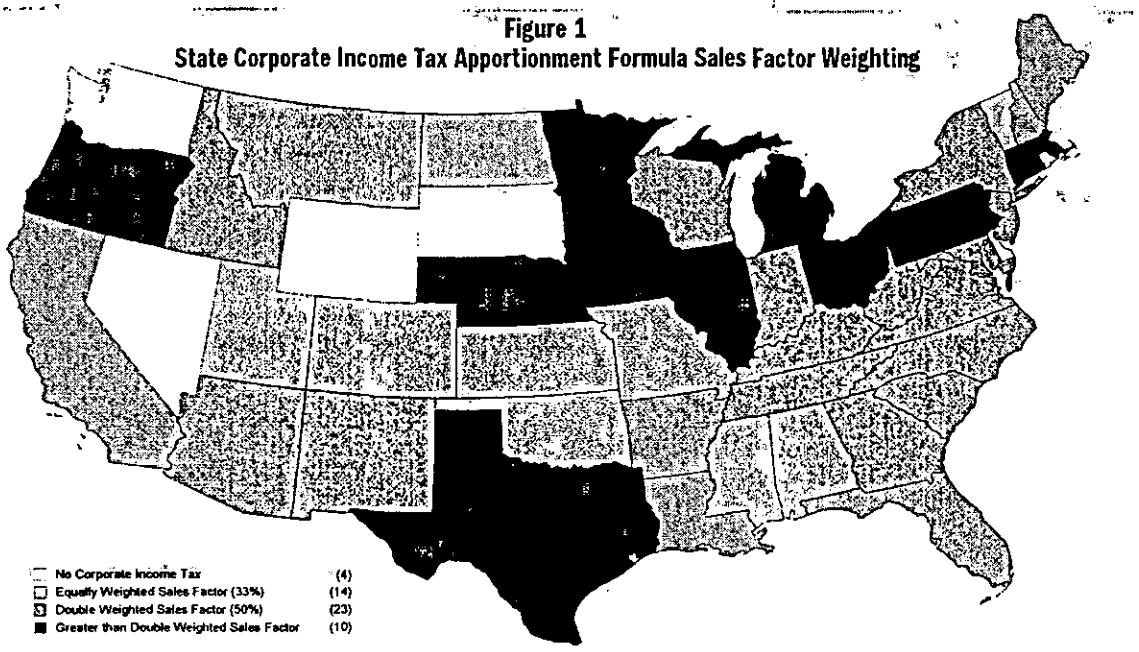
Table 1
State Corporate Income Apportionment Factor Weighting for Manufacturers, 2004*

Alabama ..... 3 Factor	Louisiana ..... Double Weighted Sales	Ohio ..... 60% Sales, 20% P & P
Alaska ..... 3 Factor	Maine ..... Double Weighted Sales	Oklahoma ..... 3 Factor
Arizona ..... Double Weighted Sales	Maryland ..... Sales Only	Oregon ..... 80% Sales, 10 % P & P
Arkansas ..... Double Weighted Sales	***Massachusetts ..... Sales Only***	Pennsylvania ..... 60% Sales, 20% P & P
California ..... Double Weighted Sales	Michigan ..... 90% Sales, 5% P & P	Rhode Island ..... 3 Factor
Colorado ..... 3 Factor	Minnesota ..... 75% Sales, 12.5% P & P	South Carolina ..... Double Weighted Sales
Connecticut ..... Sales Only	Mississippi ..... 3 Factor	South Dakota ..... No State Income Tax
Delaware ..... 3 Factor	Missouri ..... Sales Only	Tennessee ..... Double Weighted Sales
Florida ..... Double Weighted Sales	Montana ..... 3 Factor	Texas ..... Sales Only
Georgia ..... Double Weighted Sales	Nebraska ..... Sales Only	Utah ..... 3 Factor
Hawaii ..... 3 Factor	Nevada ..... No State Income Tax	Vermont ..... 3 Factor
Idaho ..... Double Weighted Sales	New Hampshire ..... Double Weighted Sales	Virginia ..... Double Weighted Sales
Illinois ..... Sales Only	New Jersey ..... Double Weighted Sales	Washington ..... No State Income Tax
Indiana ..... Double Weighted Sales	New Mexico ..... Double Weighted Sales	West Virginia ..... Double Weighted Sales
Iowa ..... Sales Only	New York ..... Double Weighted sales	Wisconsin ..... Double Weighted Sales
Kansas ..... 3 Factor	North Carolina ..... Double Weighted sales	Wyoming ..... No State Income Tax
Kentucky ..... Double Weighted Sales	North Dakota ..... 3 Factor	Wash. DC ..... 3 Factor

*Reflects current law and legislated changes for 2004

Figure 1 illustrates the geographic distribution of sales factor weighting. States using doubly or greater weighted sales factor formulas are concentrated in industrial states in the Northeast and upper Midwest, which represent a large portion of the nation's manufacturing. Of the top 10 manufacturing states, 5 use sales as the dominant or single factor.

Figure 1
State Corporate Income Tax Apportionment Formula Sales Factor Weighting



II. Manufacturing's Importance in the Massachusetts Economy

As shown in Figure 2, manufacturing employment in Massachusetts has been falling relative to manufacturing employment in the U.S. and among the other New England states since the mid-1980s. Figure 2 plots employment levels relative to the number of manufacturing jobs in 1969 (index value equal to 1.0). For example, the line for Massachusetts shows that by 1999, in-state manufacturing employment was only 65 percent of the level in 1969. In other words, manufacturing jobs fell by 35 percent, far exceeding the decline in U.S. manufacturing employment and the 30 percent drop in other New England states.

The Massachusetts legislature was reacting to the steep drop in manufacturing jobs from 1985 to 1995 when they adopted the single sales factor formula. Since the mid-1990s, the fall in manufacturing jobs in Massachusetts has more closely followed the trend throughout the U.S. Figure 3 shows that Massachusetts was affected by the region-wide decline in manufacturing employment in the Northeast.

Even with the reduction in Massachusetts manufacturing over the last two decades, durable and non-durable manufacturing remain important components of the Massachusetts economy. Manufacturing accounts for almost 383,000 jobs in Massachusetts, 11 percent of total private-sector jobs in the state today. But employment understates the importance of manufacturing to the Massachusetts economy. Because of the high value-added in manufacturing, over 20 percent of all the income paid to workers and investors in Massachusetts comes from the manufacturing sector. As seen in Figure 4, manufacturing wages in Massachusetts reflect the very high productivity of Massachusetts employees in this sector. Massachusetts manufacturing wages have risen steadily relative to the U.S. average since the mid-1980s and were over 20 percent higher than the U.S. average by 2001.

Figure 2
Manufacturing Sector Employment, 1969 - 2002

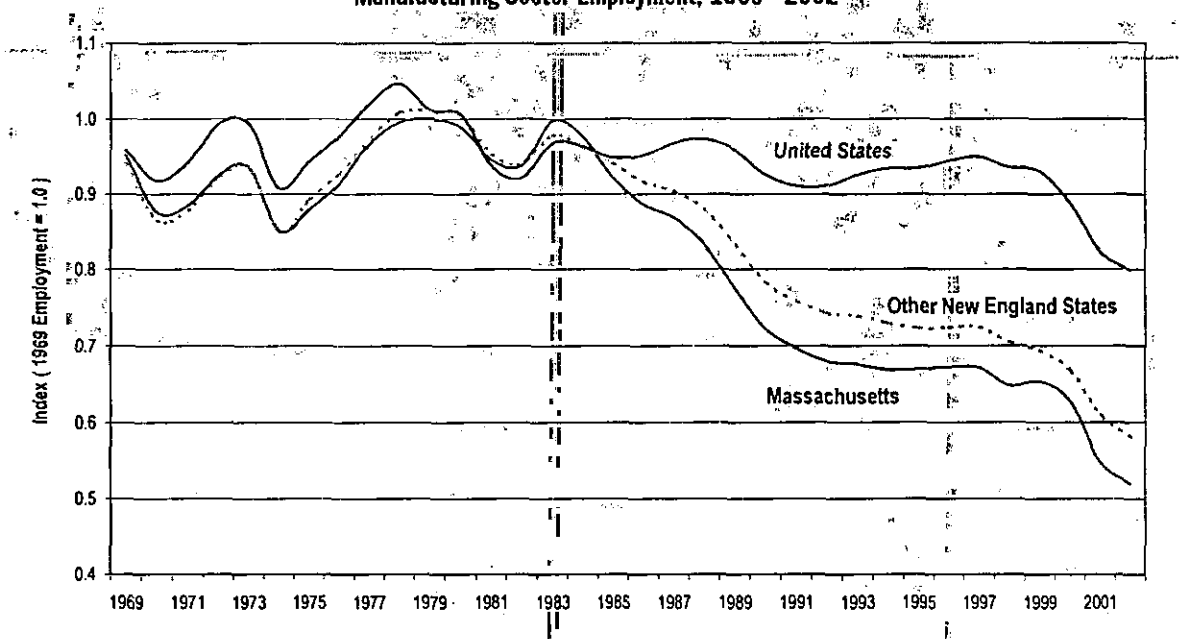


Figure 3
Manufacturing Employment Percentage Change 1969-2001

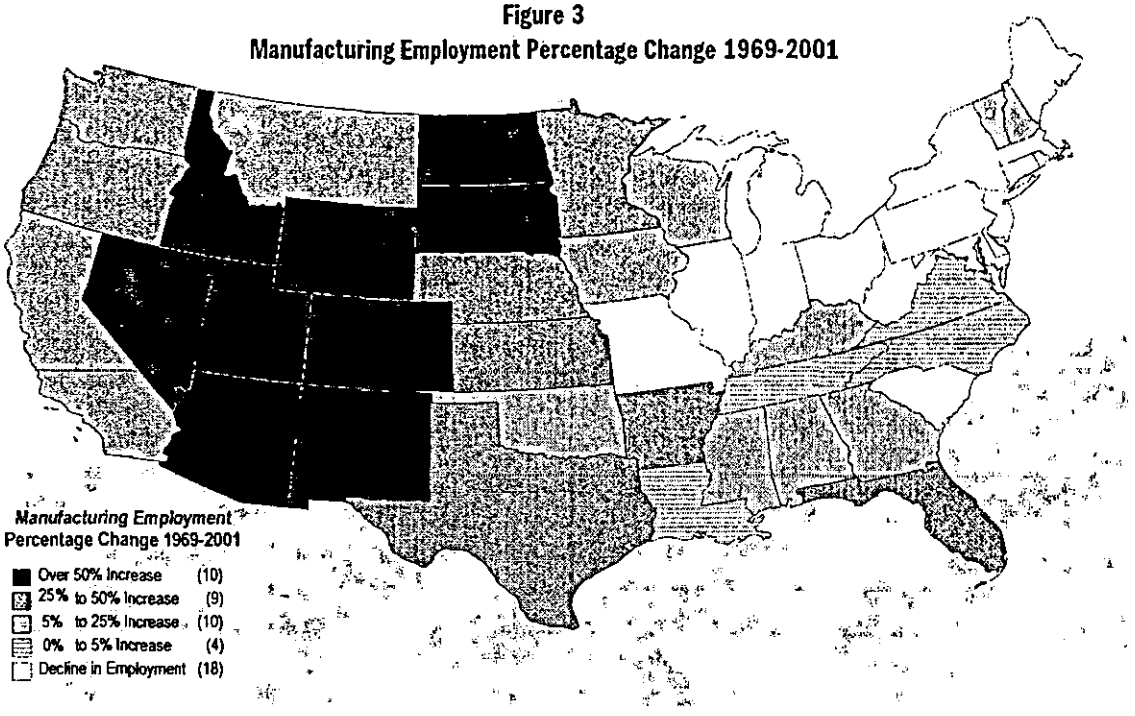
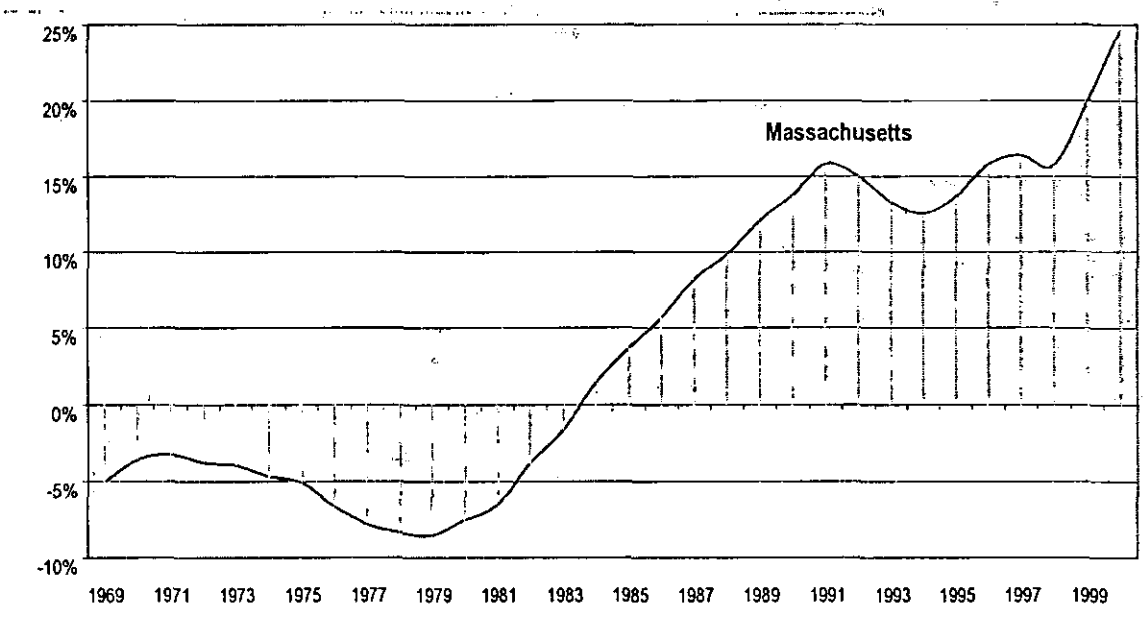


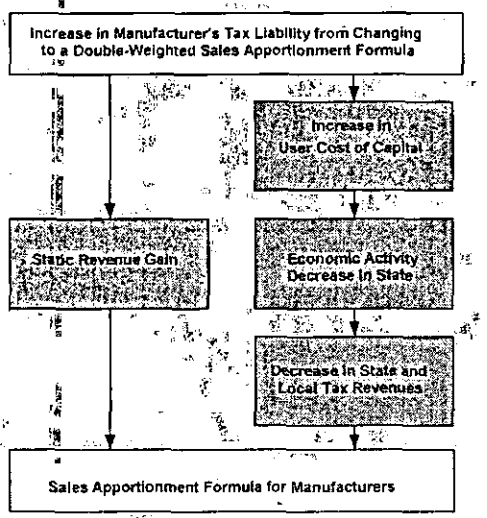
Figure 4
Massachusetts Average Manufacturing Wage Relative to U.S., 1969 - 2001
(The Percentage Difference from the U.S. Average Wage)



III. The Economic and Revenue Effects of the Sales-Only Apportionment Formula for Manufacturers

The single sales factor apportionment formula provides a significant incentive for manufacturers to expand or retain jobs and investment in Massachusetts. This incentive has increased the level of in-state employment and income compared to the level of economic activity that would have occurred under the prior law double-weighted sales factor formula. This study estimates the additional private- and public-sector benefits attributable to the sales-only formula that would be lost if the state returns to a double-weighted apportionment formula for manufacturers.

Figure 5
Estimating the Net Fiscal Impact of Reverting to Double-Weighted Sales Apportionment



To estimate the economic and fiscal impacts of switching from the sales-only to a double-weighted formula we:

1. Estimated the increase in corporate excise taxes (based on income) if the apportionment formula is returned to the prior double-weighted sales factor apportionment formula,

2. Simulated the negative impact of the higher corporate excise taxes paid by Massachusetts firms on jobs, income, and economic activity, and

3. Determined the net effect of the apportionment formula change on state and local government tax revenues: the difference between a) higher corporate excise taxes (the "static" revenue impact) due to the formula change, and b) *lower state and local taxes due to a state economy weakened* by the static corporate tax increase (the "dynamic" revenue impact).

Economic Impacts

We estimate that the switch from the sales-only apportionment formula for manufacturers to a double-weighted formula would increase corporate excise taxes by $52.5 million in 2003, based on data compiled by the Massachusetts Department of Revenue.[4]

As illustrated in Figure 5, the corporate tax increase was then used as a policy variable input to a model of the Massachusetts state economy to estimate the negative impact of the formula change on the private-sector economy.[5] *The model is a dynamic economic forecasting and policy simulation tool that captures economic interactions of the* Commonwealth's industries, as well as changes in Massachusetts' competitive position among the states.

[4] Commonwealth of Massachusetts, Department of Revenue, Report *on Section-38 Manufacturers (MGL, Chapter 63, Section 38) Year 1996.* This is the latest report currently available on the impact of the sales-only manufacturing formula and relies on taxpayer information to estimate their tax savings due to the alternate formula. We projected this figure, based on the first year phase-in of the new formula to 2003 amounts with a 100 percent single sales factor formula.

[5] The Massachusetts Department of Revenue has also used the REMI model in dynamic impact estimations of corporate tax policy alternatives. See Alan Clayton-Matthews, *State Tax Notes*, September 20, 1993.

The total change in manufacturing sector corporate taxes was translated into a change in the effective corporate tax rate for manufacturers. The increase in manufacturers' effective corporate tax rate raises their cost of capital. Because of the higher cost of doing business in Massachusetts, the corporate tax increase results in decreased employment, investment, and income in the state.[6]

The analysis described above shows that economic impact of the manufacturing apportionment formula is significant in terms of jobs and personal income. Table 3 shows that the manufacturing apportionment formula is associated with nearly 6,200 jobs and almost $372 million of Massachusetts resident personal income.

Table 3
The Single Sales Factor Formula's Economic Effect
(dollars in thousands)

Economic Impact	2003
Massachusetts Jobs	6,190
Resident Personal Income	$371,800

State and Local Fiscal Impacts

The sales-only manufacturing apportionment formula generates an annual cost to the Commonwealth from forgone corporate income tax revenues. As noted above, we estimate that the amount of corporate tax reduction attributable to the alternative formula, the "static" cost of the provision, is $52.5 million. The results presented below are estimates of the net fiscal impact of reverting to the double-weighted sales formula. Therefore, the positive dynamic tax benefits of the alternative formula are presented as negative impacts, representing the revenue that would be forgone if the double-weighted formula were reinstated.

As shown in Table 4, Massachusetts' net state revenue gain from eliminating the alternative formula is less than the total additional liabilities of Massachusetts firms caused by the reduction in state and local taxes. due to the reduction in state and local taxes due to reduced economic activity, referred to as the "dynamic" fiscal impact of the change. The net impact is sum of the impacts of the net static change in corporate taxes and the dynamic reduction in tax revenues resulting from decreased economic activity.

Table 4
Manufacturing Apportionment Effect, 2003
(dollars in millions)

Tax Impact	2003
A. Corporate Tax Revenue Impact	**$52.5**
B. State Dynamic Tax Impacts	
General Sales and Gross Receipts	($9.7)
Individual Income Tax	($16.9)
Corporate Net Income	($1.3)
License and Other Taxes	($1.2)
Total State Dynamic Tax Impact	**($29.1)**
Net State Tax Impact (A+B)	**$23.4**
C. Local Dynamic Tax Impacts	
Property	($11.9)
Selective Sales and Other Taxes	($0.3)
Total Local Dynamic Tax Impact	**($12.2)**
Net State and Local Impact (A+B+C)	**$11.1**

Subtracting the Commonwealth's dynamic revenue reduction ($29.1 million) from the estimated increased liabilities of Massachusetts corporations ($52.5 million), the net increase in Commonwealth revenues is $23.4 million. The decreased economic activity resulting from a change to a double-weighted sales formula also results in decreased local revenues of $12.2 million.

To fully quantify the impact of the single-sales factor formula increased public spending on unemployment compensation and welfare payments should be considered. The cost of these services for 6,200 displaced workers is estimated to be $9.9 million annually until workers relocate or find other jobs. The remaining net budgetary impact, $1.2

[6] The negative impact of the switch from the sales-only formula is estimated as the difference in employment, income, and other key economic variables between the baseline estimate and the simulation with higher corporate excise taxes. While the negative impacts are expected to grow over time we report the results in 2003 dollars in the report.

million would be eliminated by reductions in income taxes paid by out-of-state manufacturers with insignificant presence in Massachusetts.

Appendix A: Description of the Massachusetts Manufacturer's Single Sales Factor Apportionment Formula

Massachusetts is one of eight states that have adopted single sales factor apportionment.

Under single sales factor apportionment, a taxpayer's income is generally attributed to the various states based solely on the percentage of overall sales made to customers in each state. Massachusetts requires corporations that fall within the definition of a "section 38 manufacturer" to use single sales factor apportionment. Defense contractors and mutual fund service corporations are also required to use single sales factor apportionment. This appendix focuses on the rules applicable to section 38 manufacturers.[7]

This Appendix refers to section 38 manufacturers and manufacturers interchangeably. The term section 38 manufacturer is a term used in the Massachusetts regulations to distinguish manufacturers required to use single sales factor apportionment and manufacturing corporations that are entitled to certain tax benefits (ITC and local property tax exemptions) that are not relevant to this memo. A detailed definition of the term is provided below in the definitions section.

Mechanics

The application of single sales factor apportionment is relatively straightforward. Under single sales factor apportionment, net income subject to tax in Massachusetts is determined by multiplying overall net income by the apportionment sales factor. The apportionment sales factor is a fraction, the numerator of which is Massachusetts sales and the denominator of which is overall sales everywhere. For sales of tangible goods (e.g., manufactured items) a Massachusetts sale occurs when the goods are delivered to a customer located in Massachusetts. Tangible goods shipped to customers outside Massachusetts are not Massachusetts sales unless the "throwback" rule applies.[8] Sales of services are generally treated as sales in the state where the greater portion of the service is performed.

Single sales factor apportionment is based entirely on the sales factor. Neither the property nor the payroll factors are used (except during the phase-in period described below).

History

The single sales factor apportionment rules were added in 1995 and were phased in over five years under the schedule set forth below. The intent of the statutory amendment was to preserve and create manufacturing jobs and increase investment in Massachusetts by reducing taxes for in-state manufacturers through changes in apportionment formula. The three-factor apportionment formula, which had previously applied to all corporations, including manufacturers, was viewed as discouraging investment and job creation in the Commonwealth by "penalizing" increases in property and payroll. Specifically, the three-factor formula bases a taxpayer's Massachusetts apportionment on the amount of property, payroll and sales attributed to Massachusetts as a percentage of overall property, payroll and sales. (The three-factor formula employs a double-weighted sales factor.) Manufacturers with physical plants located in

[7] Note that the economic and fiscal impact estimates in this report include both Section 38 manufacturers and defense contractors as "manufacturers."

[8] If a seller is not taxable in the state where the goods are delivered, the throwback rule treats the sale as a Massachusetts sale unless the sale was made by a sales office located outside Massachusetts. Sales will be attributed to an out of state sales office if the salesman is located at or reports to that office and the sale is approved at that office. The throwback rule does not apply to foreign sales.

Massachusetts tended to have high property and payroll factors and thus had more of their income attributed to Massachusetts than their out-of-state competitors, whose plants and employees were located elsewhere. Moreover, the three-factor formula had the perverse effect of causing a manufacturer's Massachusetts apportionment percentage (and hence its tax bill) to increase with each additional item of equipment placed in service in Massachusetts and each new employee hired in the Commonwealth. Thus, the switch to single sales factor apportionment was intended to bolster Massachusetts investment and employment by (i) reducing taxes for in-state manufacturers and (ii) removing disincentives for investment and hiring in the Commonwealth. It had the additional effect of increasing Massachusetts taxes for many out-of-state manufacturers.

Benefit for In-State Manufacturers

Single sales factor apportionment tends to reduce the amount of income attributed to Massachusetts for in-state manufacturers compared to the amount of income that would be attributed to the Commonwealth under the three-factor, double-weighted formula that applied under prior law. This is because Massachusetts-based manufacturers are likely to have high levels of property and payroll in Massachusetts relative to overall property and payroll and thus have high property and payroll apportionment factors. Single sales factor apportionment ignores the property and payroll factors and uses only the sales factor, which for an in-state manufacturer with a multi-state customer base is likely to be significantly lower than the property and payroll factors. Thus, the in-state manufacturer's Massachusetts apportionment percentage is reduced and less of the manufacturer's income is taxed by Massachusetts than would be the case under the three-factor formula.

Potential Disadvantage for Out-of-State Manufacturers

Note that the use of single sales factor apportionment is compulsory for all section 38 manufacturers. Thus, section 38 manufacturers located outside Massachusetts are required to use single sales factor apportionment even when it does not benefit them. It will frequently be the case that single sales factor apportionment will result in a larger amount of an out-of-state manufacturer's income being attributed to Massachusetts. This is because single sales factor apportionment ignores an out-of-state manufacturer's Massachusetts property and payroll factors, which are likely to be very low as the corporation's physical plant and employees will be located outside the Commonwealth. Instead, single sales factor apportionment focuses entirely on the Massachusetts sales factor, which for an out-of-state producer with a multi-state customer base is likely to be higher than the property and payroll factors. Thus, the out-of-state manufacturer's Massachusetts apportionment percentage cannot be diluted by out-of-state property and payroll and, therefore, tends to increase. As a result, more of the out-of-state manufacturer's income is taxed by Massachusetts than would be the case under the three-factor formula.

Phase - In

Prior to the 1996 tax year, all corporations, including section 38 manufacturers, used the following double-weighted sales factor Massachusetts apportionment formula: Sales Factor-50%, Property Factor-25% and Payroll Factor-25%. For tax years beginning on or after January 1, 1996, the following formulas were created to gradually increase the weight of the sales factor relative to the property and payroll factors over a 5-year period for section 38 manufacturers:

Historical Massachusetts Manufacturing Apportionment Formula Weights

1995:	Sales Factor-50%	Property Factor-25%	Payroll Factor-25%;
1996:	Sales Factor-60%	Property Factor-20%	Payroll Factor-20%;
1997:	Sales Factor-70%	Property Factor-15%	Payroll Factor-15%;
1998:	Sales Factor-80%	Property Factor-10%	Payroll Factor-10%;
1999:	Sales Factor-90%	Property Factor-5%	Payroll Factor-5%;

2000: Sales Factor-100%.

Definitions

Section 38 Manufacturer. Generally, a corporation other than a utility, defense or mutual fund service corporation is a section 38 manufacturer for any taxable year if 1) it is engaged in manufacturing during the taxable year, and 2) its manufacturing activity during the taxable year is substantial. A corporation that meets these two requirements is a section 38 manufacturer for the taxable year regardless of whether, or to what extent, it conducts its manufacturing activities in Massachusetts. All section 38 manufacturers must use the single sales factor apportionment formula.

Substantial Manufacturing. *A corporation's manufacturing activity is considered "substantial" for any taxable year* if the corporation meets any one of the following five tests:

1. The corporation derives 25% or more of its receipts for the taxable year from the sale of manufactured goods that the corporation manufactures (The Receipts Test); or
2. The corporation pays 25% or more of its payroll for the taxable year to employees working in manufacturing operations and derives 15% or more of its receipts for the taxable year from the sale of manufactured goods that the corporation manufactures (The Payroll/Receipts Test); or
3. The corporation uses 25% or more of its tangible property in manufacturing during the taxable year and derives 15% or more of its receipts for the taxable year from the sale of manufactured goods that the corporation manufactures (The Tangible Property/Receipts Test); or
4. The corporation uses 35% or more of its tangible property in manufacturing during the taxable year (The Tangible Property Test).

Source Materials

Statute:	Mass. Gen. Laws ch. 63, § 38
Regulation:	830 CMR 63.38.1 830 CMR 58.2.1

Appendix B: Description of the REMI Massachusetts Economic Model

The REMI model incorporates information from the U.S. Bureau of Economic Analysis, the Bureau of Labor Statistics, the Department of Energy, and other public sources to develop a detailed model of the Massachusetts economy. The model includes an input-output structure that describes commodity flows from producers to intermediate and final consumers. The total industry purchases of commodities, services, employment compensation, value added, and imports is equal to the value of the commodities produced. Purchases for final use (final demand) drive the model. Industries producing goods and services for final demand purchase goods and services from other producers. These other producers, in turn, purchase goods and services. This buying of goods and services (indirect purchases) continues until leakage from the region (imports and value added) stop the cycle.

The model summarizes these complex interactions and uses the data to estimate the total economic impact of the employment, investment and export sales related to the eligible industries in Massachusetts. The REMI model has detailed information for each of 53 sectors of the state economy, including communications. The model is used to establish a baseline economic forecast for the state under current law. Policy variables are then used to model the expected impacts of the credit's elimination, as described in the text.

HENRY DORMITZER
COMMISSIONER

The Commonwealth of Massachusetts
Department of Revenue
Office of the Commissioner
P.O. Box 9550
Boston, MA 02114-9550

October 29, 2007

Ms. Monica C. Garlick
Research Director
Joint Committee on Economic Development and Emerging Technologies
State House, Room 42
Boston, MA 02133 - 1020

Dear Ms. Garlick:

You requested that the Department of Revenue provide estimates of the revenue impact of H.4234, "An Act Providing For the Investment in and Expansion of the Life Sciences Industry in the Commonwealth". The bill proposes a number of tax incentives, as summarized in a document sent to you by DOR's Legal Division on October 23, 2007 (see attached). These tax incentives would be provided only to "certified life sciences projects", upon joint approval by the Secretary of Housing and Economic Development and the Secretary of Administration and Finance. While the legislation itself does not establish an annual dollar cap for the tax incentives, the Administration has stated that the annual cap for all approved tax incentives would be $25 million. The Department of Revenue estimates that there would be a large enough supply of certified life sciences projects to reach the $25 million cap each year. However, since the value of each proposed tax incentive under the cap would be subject to the approval of the Secretaries of Housing and Economic Development and Administration and Finance, and the Secretaries would adjust their approvals of particular tax incentives to stay within that cap, it is impossible for DOR to estimate the value of a particular tax incentive for a particular year. It should also be noted that according to the Governor's proposal, a particular project would not necessarily receive approval for all available tax incentives, but only those and only to the extent specified in the certification.

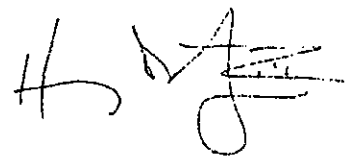
You also requested that DOR estimate the value of each proposed tax incentive if the $25 million annual cap were removed and there were no project-specific approval required. The attached table shows DOR's estimates of the (static) revenue loss associated with changing the Governor's proposal from one in which the incentives would be project-specific and subject to the approval of the Secretaries of Housing and Economic Development and Administration and Finance to one in which the incentives would be freely available to all life sciences companies without prior approval by the Commonwealth. While DOR has attempted to estimate the revenue impact of each of the tax incentives, we did not have enough information available to us to estimate the revenue impact of

extending the net operating loss carryover from the current 5 years to 15 years for life science companies (proposal number 4 on the attached list) or the proposal to make the research and development tax credit refundable (proposal number 6b on the attached list). Furthermore, the Governor's proposal to grant "research and development" status to certified life sciences projects (proposal number 6a on the attached list), which would qualify those projects for sales tax exemptions, is integrally related to the project certification process. To separate it from the certification process would fundamentally change the proposal, requiring additional assumptions regarding the types of companies that would qualify for research and development status. Therefore, DOR was not able to estimate the revenue impact of converting this tax incentive to one not subject to a certification process and an annual cap.

Please also note that the attached estimates are "static", meaning that they do not take into account the additional tax revenue generated by new economic activity induced by the tax incentives. To the extent that economic activity in the life sciences industry is greater as a result of the tax incentives, the revenue reductions shown would be offset by additional tax revenue collected by the Commonwealth. The capped $25 million estimate is also static, and would be lower if the additional economic activity generated by the incentives were taken into account.

If you have any questions concerning these estimates, please contact me (at 617-626-2201), or Howard Merkowitz, Director of the Office of Tax Policy Analysis (at 617-626-2100).

Sincerely,



Henry Dormitzer
Commissioner

Attachments (3)

cc: Robert Brandt, Joint Committee on Economic Development and Emerging Technologies

Estimates of Life Sciences Tax Incentives

Assumed to be Available to All Life Sciences Companies

(Different From Governor's Proposal, Which is Project-Specific and Subject to Annual Cap)

Effective Date: Assumed to be 1/1/2008

	Tax Incentive	Annualized Revenue Impact (Static Estimate)
1	Refundable 10% Investment Tax Credit (ITC) for Life Sciences Companies	-$20.5 Million to -$24.5 Million
2	Additional ITC for Projects Located in Economic Opportunity Areas	-$5.5 Million to -$8.0 Million
3	Life Sciences Human Drug User Fee Credit	-$13.6 Million to -$20.4 Million
4	Net Operating Loss (NOL) Carryover for Life Sciences Companies Extended from Current 5 Years to 15 Years	Estimate not Available
5	Eliminate MA Throwback Provision for Life Sciences Companies	-$3.0 Million to -$6.0 Million
6	a) Certified projects considered Research and Development Entities for the Purposes of Sales Tax Exemptions	Estimate Not Applicable - Proposal is Integral to Certified Projects
	b) Refundability of Research and Development Tax Credit	Estimate Not Available
7	Sales Tax Exemption Created for the Expansion of Utility Support Systems for Life Sciences Companies	-$1.0 Million to -$6.0 Million

Mass. Dept. of Revenue
October 19, 2007

Tax Incentives in Governor Patrick's Life Sciences Legislative Proposal

On July 19, Governor Patrick filed a legislative proposal to encourage investment in and expansion of the life sciences industry in Massachusetts. The proposed legislation, assigned docket number H 4234, would provide bond funding for capital projects and funds for fellowships, research grants and loans, and workforce training programs. In addition, the proposal would provide for certified life sciences projects and would award tax incentives to Massachusetts businesses engaged in life sciences.

Of the seven tax incentives in the proposal, three are tax credits, available to both individuals and corporations, and four are tax benefits that take other forms. The Secretary of Housing and Economic Development may award certification to an applicant life sciences sector business that is located in the Commonwealth and engaged in research, development or manufacturing. To be certified as a "certified life sciences project," a business must be engaged in the life sciences, engaged in research, development or manufacturing, and develop a new or expanded facility in the commonwealth, thereby increasing the number of its permanent full-time employees. The project's certification may be revoked if the business does not meet at least 70% of its employment goals as outlined in its proposal. The tax benefits may be awarded in some combination, on a project by project basis and to the extent provided, by the Secretary of Housing and Economic Development and the Secretary of Administration and Finance, acting jointly. The tax incentives are summarized below.

1. Life Sciences Investment Incentive Tax Credit. (Bill Sections 14 & 21)

The Life Sciences Investment Incentive Tax Credit is a 10% refundable tax credit that may be given to any certified life sciences project (individual or corporation) for 10% of the costs of certain property associated with a project. If the project so chooses, it may carry over the tax credit for 10 years, instead of taking the refund in the first year. Section 14 would amend section 6 of c. 62, the personal income tax chapter; Section 21 would add a new section 38U of c. 63, the corporate excise chapter.

2. Additional Credit for Projects Located in Economic Opportunity Areas. (Bill Sections 14 & 21)

In addition to establishing the Life Sciences Investment Tax Credit, sections 14 & 21 allow a certified project to be eligible for an additional 2% tax credit for projects located in Economic Opportunity Areas, as defined in subsection (g) of section 31A of chapter 63.

3. Certified Life Sciences Project User Fee Credit. (Bill Sections 15 & 17)

The proposed User Fee Credit is a 100% refundable credit against the fees paid by a project for application to the USFDA for a human drug application or supplement which was primarily researched and developed in Massachusetts. Section 15 amends section 6 of chapter 62; section 18 amends chapter 63 by adding a new section 31M.

4. Net Operating Loss (NOL) Carryover for Certified Life Sciences Projects Extended from the Current 5 Years to 15 Years. (Bill Section 16)

Currently, all corporations are allowed to carry over NOL deductions for 5 years. If a certified life sciences project experiences losses over a longer period of time than 5 years, the project may carry over those losses for up to 15 years. Section 16 amends section 30 of chapter 63.

5. Massachusetts "Throwback Sales Provision" Eliminated For Certified Life Sciences Projects. (Bill Section 18)

For purposes of apportionment of corporation excise tax, sales by certified projects of products manufactured in Massachusetts may be "sourced" to a customer's state outside of Massachusetts without being subject to the "throwback" rule in chapter 63 that generally requires sourcing of sales to Massachusetts in certain cases where the seller is not taxable in the customer's state. Section 18 amends section 38 of chapter 63.

6. Certified Projects Considered Research and Development Entities for the Purposes of Sales Tax Exemptions; R&D Credits May Be Refundable (Bill Sections 19 & 22; section 20)

Certified projects will be deemed to be research and development corporations, to the extent provided in the certification, without having to meet the proof requirements of that classification, in order to be exempt from the sales tax. Section 19 creates the exemption for domestic corporations and section 20 creates the exemption for foreign corporations. In addition, section 20 provides that the current research and development tax credit may be refundable for certified life sciences projects.

7. Sales Tax Exemption Created for the Expansion of Utility Support Systems Associated with a Certified Life Sciences Project. (Section 23)

This provision provides that utility support system costs associated with a certified life sciences project may be exempted from the state sales tax. Section 23 amends section 6 of chapter 64H.

245776

Haddad, William (HOU)

From: Antonellis, Peter (HOU)
Sent: Wednesday, January 23, 2008 3:13 PM
To: Haddad, William (HOU)

Billy,

Below is the extent of our recommendations to Chairman Bosley concerning the LSI and tax policy.

Tax Investment Incentives

In reference to any tax incentive provisions that are approved by the legislature, I believe any tax policy approved by the legislature should be black and white.

I have no problems with the administration's attempt to carve out specific tax policies for the life sciences industry. Rather than awarding these tax incentives to companies that are deemed to qualify as life sciences companies, I believe it better to identify within the legislation what qualifies a business as a life sciences company. This way the determining factors are set within the law. Certifying each applicant as a life sciences approved company one by one is needlessly wasteful.

As the financial outlook of the Commonwealth continues to change daily, I find it unlikely that all 7 tax incentive provisions will be passed. If this is the case I believe increasing the NOL Carry Forward to either 10 or 15 years would be the best option to encourage business development. I have taken meetings with several companies that have stated that of the many provisions mentioned in the Life Sciences Initiative, this is the one they most want.

Peter S. Antonellis
Legislative Aide
Chairman Michael Rodrigues
Room 43, State House
Boston, MA 02133
(617) 722-2030

Draft Amendments to H4234
An Act *Providing for the Investment in and Expansion of the Life Science* Industry in the Commonwealth

Section 3 or 4: Adds to this section of capital expenditures totaling $500,000,000 a provision that requires the companies to whom the infrastructure improvement will accrue benefit to provide to the Life Science Industry revolving credit facility/trust shares of equity or warrants or options that amount to 0.5% of the value of the infrastructure improvement cost.

Section 12: Amends section by striking references to grants and specifies that all investments to universities, colleges, public instrumentalities companies, and other entities should take the form of securities that are low cost loans during years 0-5, then low- cost convertible bonds from years 6-20.

Section 14: Amends the Life Sciences Investment Incentive Tax Credit to include a provision that mandates that taxpayer who utilize the tax credit herein at the 10% rate of the value of the property, shall also provide to the Life Science Industry revolving credit facility/trust either (a) equity shares equivalent to 0.5% of the value of the property, or (b) the establishment and perpetuation for at least 10 years of FTE slots in accordance with the following table:

ITC: FTE calcs
value of one FTE $ 50,000

Property Value	ITC percentage	ITC amount	FTE equivalent
$ 5,000,000	10%	$ 500,000	10
$10,000,000	10%	$ 1,000,000	20
$15,000,000	10%	$ 1,500,000	30
$20,000,000	10%	$ 2,000,000	40
$25,000,000	10%	$ 2,500,000	50
$30,000,000	10%	$ 3,000,000	60
$35,000,000	10%	$ 3,500,000	70
$40,000,000	10%	$ 4,000,000	80
$45,000,000	10%	$ 4,500,000	90
$50,000,000	10%	$ 5,000,000	100

Section 15: delete section on FDA application and user fee credits

Section 19, 21, 22: Amends the section related to R&D tax credits to include a provision that mandates that taxpayers who utilize the tax credit herein at the 10% rate of the value of the property, shall also provide to the Life Science Industry revolving credit facility/trust either (a) equity shares equivalent to 0.5% of the value of the property, or (b) the establishment and perpetuation for at least 10 years of FTE slots in accordance with the table above.

Section 24: Adds a new section that mandates companies who meet the following criteria must provide warrants or shares or options on shares (at a strike price equivalent to 75% of the share price at the time of the event) to the Life Science Industry revolving credit facility/trust:

(a) is a for profit entity in accordance with Massachusetts tax laws;
(b) has been awarded a patent for a product;
(c) has sale proceeds of such product;
(d) has licensing fee proceeds related to such product;
(e) has been the beneficiary at any time in the past of Massachusetts tax credits, infrastructure developments, loans or convertible bonds, either directly from the Commonwealth general fund as authorized by this law or via the Life Science Industry revolving credit facility/trust.

The companies that meet the criteria above must contribute warrants or shares or options which have a market value of 0.25% of the revenue attributable to the product sales or licensing fees.

Section 25: Adds a new section about management of the Life Science Industry revolving credit facility/trust by the Life Science Center Board, in conjunction with the PERAC, and management of the disbursements of dividend income, interest, or proceeds from the sale of equity shares, which are to be funneled back into the life science industry in Massachusetts in accordance with other provisions of this law.

Contact: Jenny Nathans, 617-722-2460
Office of Rep. Tom Conroy

Massachusetts Life Sciences Initiative
Tax Provisions

Issue: Federal Orphan Drug Language

The term "orphan drug" refers to a drug that will be used to treat a rare disease or condition. The Federal Orphan Drug Act (ODA) provides for granting special status to a product to treat a rare disease or condition upon request of the company.

The credit is available for testing expenses for orphan drugs. **Orphan drugs are drugs, vaccines, diagnostic drugs, or preventive drugs, used to treat rare diseases or conditions**. A rare disease or condition is defined as one which:

> (A) affects less than 200,000 persons in the United States, or
>
> (B) affects more than 200,000 persons in the United States, but there is no reasonable expectation that the cost of developing and making available in the United States a drug for disease or condition will be recovered from sales in the United States of such drug.

The Federal Orphan Drug Tax Credit (ODTC) is normally for 50 percent of the costs of clinical testing expenses. Normally the credit is limited to clinical testing that takes place in the United States although it is available for foreign trials when there is an insufficient testing population in the US. When a Life Sciences company claims the ODTC for a drug which has Orphan status, they are required under the Code to "add back" to Federal taxable income, the amount of the credit that they claimed, this additional income is then subject to Federal tax, so the net impact of the credit is really 32.5%, not the 50% credit that is initially allowed.

Massachusetts has no such Orphan Drug credit. Thus for MA purposes, R&D expenses performed in MA are eligible for the MA R&D credit. MA allows for a 10% credit on MA R&D, but not to exceed 50% of the current years expenses, so in reality a 5% credit. However, MA requires companies to add back the amount of the MA R&D credit to MA taxable income. Thus for MA purposes, it should be clarified that the Federal ODTC add back should not be includible in the MA taxable income base, otherwise only Life Science companies that pursue Orphan Drug indications would be penalized by MA taxing them twice on the same "add back" of R&D expenses.

As good public policy the state should encourage more companies to do research and development on orphan drugs.

Massachusetts Life Sciences Initiative
Tax Provisions

Rational: The bill should provide clarity that the Federal Orphan Drug add-back does not apply for a company's Massachusetts income tax base, otherwise companies working on rare diseases are unfairly penalized by taxing them twice on the same disallowed expenses, when there was no State benefit for the Federal Orphan Drug credit. Alternatively, the state should adopt a state-based Orphan Drug credit modeled after the Federal rule and including clinical activities.

Suggested Amendment: page 18, Section 15 insert after line 42 - (8) To the extent a deduction is disallowed under (6) above, it shall not be disallowed more than once after consideration of the Federal Orphan Drug credit add back as set forth in section 280C(b) of the code. Furthermore, it shall be clarified that the amount of any Orphan Drug Credit add back, included in Federal taxable income under Section 280C(b), shall not be considered as taxable income for purposes of the Massachusetts taxable income base.

Massachusetts Life Sciences Initiative
Tax Provisions

Issue: Single Sales Factor Apportionment

In simple terms, companies must "apportion" their Federal taxable income among the states in which they operate. Historically, most states used some variation on a "three factor apportionment" method, with the three factors being an average of the company's property value, payroll costs, and sales in that state, relative to the total US amounts. This average percentage is then multiplied by the Federal taxable income for the year to roughly determine a given state's share. Over the past 15 years, many states have changed their apportionment rules to that of a "Single Sales Factor" (SSF) approach. Under this method a company allocates their Federal taxable income based only on the percentage of sales to that state for the year.

A SSF method has the result of taxing out of state companies at a much higher percentage than a traditional three factor method, because if the company has no employees and no bricks and mortar in the state, it will allocate a higher amount of its income to that state, then if it used an average of all three factors. SSF is a means of raising tax revenue on non-resident companies and reducing the tax burden of the companies that have a high percentage of employees and bricks and mortar, but ship products outside their primary state of residence.

Massachusetts has maintained the three-factor formula for apportionment, but made exceptions to the rule to certain types of companies. Massachusetts currently allows any manufacturer, defense contractor or financial services company use a single sales factor apportionment method. If the Commonwealth were to expand this to include either all Life Science companies, or at a *minimum, US Headquartered Life Science companies, it would demonstrate the* Commonwealth's commitment to expanding this high growth industry in MA. As the law currently stands, large commercial Life Science companies that do not manufacture in MA are precluded from using single sales factor apportionment, *regardless of how large their investment in MA.*

Rational: In order to compete with roughly one third of the states in the US, MA *should allow those life sciences companies with headquarters in MA eligible for a* single sales factor apportionment. The current system penalizes companies headquartered in the state relative to those that only sell products into the state (while having minimal physical presence). MA currently allows single sales factor *apportionment to all manufactures, regardless of industry, as well as defense* contractors and financial service companies. This would allow for increased investment in MA by non-US based life science companies who are expanding into the US, but maintain manufacturing in their home country, as well as *expansion into MA by other non-MA Life Science companies.*

Massachusetts Life Sciences Initiative
Tax Provisions

Proposed Amendment: Page 6, Section 7. New. Insert after line 38. "Qualified US Life Science Headquarters", an affiliated group, as defined in Section 1504(a) of the Internal Revenue Code of 1986 that derives at least 70 percent of its revenue from the sale or license of life science products or intellectual property, or the rendering of contract life sciences services, or the combination of the two, if either (1) greater than 70 percent of all commercial employees, excluding sales representatives, are Massachusetts based employees, or (2) if greater than 70 percent of all tangible property (excluding inventory), leased or owned, would be apportionable to Massachusetts in the fiscal year, not withstanding the company's ability to qualify for single sales factor apportionment.

Page 24. Insert after Line 18. New. SECTION 24. Section 38 of chapter 63 of the General Laws is hereby amended by adding after subsection (n) the following subsection:-

A qualified US Life Science Headquarters Company shall be eligible to use singles sales factor apportionment for any tax year ending after enactment.

SECTION 25. Section 38(c) of chapter 63 of the General Laws is hereby amended by inserting after "a manufacturing corporation as described in subsection (l)," the following phrase:

...a qualified US Life Science Headquarters Company, as described in chapter 23A of the General Laws, Section 63(a),

Massachusetts Life Sciences Initiative
Tax Provisions

Issue: Clinical Research

Currently Massachusetts allows companies to claim R&D credits for R&D that is performed within the state, and not for R&D performed outside of Massachusetts.

Life Sciences companies are unique in that they are legally mandated by the FDA to perform extensive clinical testing (clinical trials) for their products to prove safety and efficacy, before the FDA will approve the drug for use in humans. The FDA also mandates that the drugs be administered by a physician in a clinical setting, and that the clinical trials take place in a geographically diverse manner to add to the statistical reliability of the results. Generally, the largest R&D expenses of a Life Science company are payments to physicians to conduct these trials (investigator payments). Under the existing and proposed legislation, only payments made to Massachusetts' physicians for clinical trials would be eligible for the R&D credit. Given the size of Massachusetts relative to the rest of the country, this works out to be typically less than 5% of the clinical trial expenditures.

Rational: Under the existing MA R&D credit rules, only R&D performed in MA is eligible for the R&D credit. In terms of "discovery" type R&D, this makes perfect sense, as the employee that is conducting the experiment, is standing in one facility every day. However, the unique nature of the Life Science industry is that companies are required by the FDA to perform extensive clinical trials on a national basis. Companies cannot achieve commercial success without incurring these enormous costs over a number of years. This is unique from other industries that have the ability to choose where their R&D is performed. Life Science companies can only choose the location of discovery/ laboratory based R&D.

Life Science companies that choose to locate their US Headquarters in MA are choosing to put all of the jobs that plan and support the clinical and regulatory processes in the Commonwealth and should be provided an incentive to put these highly compensated jobs here. In this regard, a US Headquartered Life Science company is investing in MA with respect to the jobs and expenditures that are within it's control, and thus should be allowed to claim R&D credits for clinical trials performed outside of MA if they meet the US Life Science Headquarters definition. This would provide a differentiating incentive compared to other states for larger companies to located their US Headquarters and commercial operations in MA and encourage growing/successful biotech companies to stay in MA.

Proposed Amendments: Page 18, Section 15. Lines 8-9. and, with respect to Qualified US Life Science Headquarters Companies, qualified research

expenses as defined in section 41(b) of the code, to the extent they relate to legally mandated clinical trial activities not otherwise taken into account as research and development costs

Page 18. Section 15. Lines 10-15. "User fees", the monetary amount actually paid by a certified life sciences project to the U.S.F.D.A. that constitutes the fee due upon the submission of a human drug application or supplement pursuant to 21 U.S.C. Section 379h(a)(1) for a human drug, the research and development costs of which, were primarily incurred in the commonwealth, or 100 percent of such fees if the company is a Qualified US Life Science Headquarters Company

Massachusetts Life Sciences Initiative
Tax Provisions

Issue: US Headquarters

Most of the Commonwealth's tax incentives, including this Life Sciences Initiative, are aimed at providing tax incentives to companies in various industries in order to attract and retain employment in Massachusetts. This is a prudent goal and tax incentives are a proven means of modifying corporate behavior. The Life Sciences industry is a clear engine for future economic growth for any State, and there is intense competition among states to lure companies in this industry into locating or expanding in their particular State. The Governor's Life Science Initiative should be applauded in its efforts to keep Massachusetts as one of the top leaders in this industry. However, the initiative fails to capitalize on an important opportunity for corporate expansion in the Life Sciences industry, due to its' limited focus on R&D and manufacturing activities. By excluding commercial operations of Life Science companies, the incentives don't apply to companies that have preexisting manufacturing activities in another state or another country.

A unique aspect of the Life Sciences industry is that these products must be (1) tested on a broad scale in humans, (referred to as a Phase III clinical trial) before being submitted for review and approval by the FDA and (2) the drugs must be manufactured in an FDA approved facility. These two hurdles are extraordinarily time consuming and costly. A foreign company that wants to expand into the US market is likely to have their manufacturing operations overseas that are already FDA approved. Thus these companies are looking to choose a US Headquarters location from which they can plan and oversee the clinical trial process and launch the commercial sale and distribution of their products. They are neither startup drug discovery companies, nor are they necessarily US manufacturers, but they bring with them a huge potential for US employment; in white-collar jobs that on average would have salaries in excess of those of a manufacturing operation. These include the executive management level positions, regulatory affairs, clinical operations, data management, logistics and supply chain, business development, and all of the support functions for these operations, such as legal, finance, human resources, and IT. In addition, it is increasingly more common that companies contract out the manufacturing aspects of the business to a third party, since it is not their core competency, and the financial commitment to a biotech production facility is so large.

Rational: Life Sciences Companies with US Headquarters (HQ) in Massachusetts should be able to benefit from these new tax credits and incentives. The definition of a Life Science company should not be limited to R&D or manufacturing based activities alone. Rather, the greatest expansion and growth spurt occurs with commercial approval of the drug and launch of the product into the US market. Success in this industry is defined by

commercialization, by excluding this aspect of the business; the largest and most promising of the companies fall through the cracks.

Proposed Amendments:

Page 3, Section 1. (2) it is imperative for the purposes of the commonwealth's economic competitiveness that the commonwealth make the investment in life sciences research, manufacturing and commercialization a priority to leverage revenues and to encourage collaboration and innovation among public and private institutions involved in life sciences research and related applications;

Page 3, Section 1. (5) the purpose of this chapter is to establish a comprehensive life sciences program for the commonwealth, which would both support and stimulate research, manufacturing, and commercialization in this sector.

Page 6. Section 7. Insert after line 27 the following: "Commercial", non research, non development and non manufacturing related functions, including but not limited to, sales, marketing, distribution, business development, general and administrative or support functions.

Page 6, Section 7. Insert after line 38 the following: "Qualified US Life Science Headquarters", an affiliated group, as defined in Section 1504(a) of the Internal Revenue Code of 1986 that derives at least 70 percent of its revenue from the sale or license of life science products or intellectual property, or the rendering of contract life sciences services, or the combination of the two, if either (1) greater than 70 percent of all commercial employees, excluding sales representatives, are Massachusetts based employees, or (2) if greater than 70 percent of all tangible property (excluding inventory), leased or owned, would be apportionable to Massachusetts in the fiscal year, not withstanding the company's ability to qualify for single sales factor apportionment.

Page 6. Section 7. Lines 39-41 amend definition as follows: "Life sciences", advanced and applied sciences, including but not limited to, regenerative medicine, biotechnology, biopharmaceuticals, pharmaceuticals, nanotechnology, and medical devices.

Page 6. Section 7. Lines 42-44 amend definition as follows: "Life sciences sector business," a life sciences business located in the commonwealth and engaged in research, development or manufacturing, or as a Qualified US Life Sciences Headquarters Company.

Page 18. Section 15. Lines 8-9 amend as follows: "Research and development costs"; in-house research expenses within the meaning of section 41(b) (2) of the Code, and with respect to Qualified US Life Science

Headquarters Companies, qualified research expenses as defined in section 41(b) of the code, to the extent they relate to legally mandated clinical trial activities not otherwise taken into account as research and development costs.

Page 18. Section 15. Lines 10-15 amend as follows: "User fees", the monetary amount actually paid by a certified life sciences project to the U.S.F.D.A. that constitutes the fee due upon the submission of a human drug application or supplement pursuant to 21 U.S.C. Section 379h (a) (1) for a human drug, the research and development costs of which, were primarily incurred in the commonwealth, or 100 percent of such fees if the company is a Qualified US Life Sciences Headquarters Company.

Page 19. Section 17. (c) Lines 23-26 amend as follows -A certified life sciences project shall claim the credit in the taxable year in which its application for the licensure of an establishment to manufacture the human drug in the commonwealth is approved by the U.S.F.D.A. or the company is a Qualified US Headquarters company for the fiscal year.

Massachusetts Life Sciences Initiative
Tax Provisions

Issue: Certified Life Sciences Projects

Rational: While the criteria for certification as "certified life sciences project" includes both employment and ROI targets, given the high-risk nature of the life sciences industry and businesses that flow from it, the criteria for de-certification should not include the ROI component.

The current employment target required for certification as a "certified life sciences project" is 25%. For small companies a 25% increase in employees may very well be achievable, but for a large company with hundreds of employees that required target based on total company employees is not likely to be achieved. The bill should contemplate the employment increase target for staff within the area of expertise that the grants are awarded (eg R&D in one therapeutic area) rather than total employees.

The revocation of classification as a "certified project" due to missing an ROI target should be removed. The clawback provision related to a de-certified project should also be removed. Given the high-risk nature of the industry, if a company has not been able to meet its targets it is most likely unable to pay back the money it has received as a refundable credit.

Proposed Amendments: Page 11- Lines 226-245, Page 12. Lines 246-278 Section 7. iii (B) (2). The certification of a project may be revoked only by the secretary of housing and economic development after an independent investigation and determination that representations made by the life sciences sector business in its project proposal are materially at variance with the conduct of the life sciences sector business subsequent to the certification; provided, however, that the department of business development shall review such certified life sciences project at least once every year; provided, further, that where the actual return on investment is less than 70 percent of the return on investment projected in the project proposal, then this shall be deemed a material variance for the purposes of a revocation determination.

A notice of decertification shall specify the date on which the decertification is effective, which may be the date of such notice or any earlier date on which the secretary of housing and economic development determines that the material variance commenced. In the event of such decertification, the commissioner of revenue shall, as of the effective date of the decertification, disallow any credits, exemptions or other tax benefits as may have been allowed by the original certification of tax benefits pursuant to this section. In addition, any credits allowed pursuant to the certification under this section shall be recaptured in a

manner similar to that provided under section 31A of chapter 63 as would apply when property is disposed of or ceased to be in qualified use before the end of its useful life or, if applicable, before the end of the year in which the credit is to be taken. In the event that the original certification allowed sales and use tax exemptions under subsection 6(s) of chapter 64H, the purchaser shall accrue use tax as of the date of the decertification on a portion of the sales price on which exemption was claimed that is proportionate to the remaining useful life of the property. Nothing in this section shall limit any other legal remedies available to the commonwealth against the life sciences sector business. Annually, on or before the first Wednesday in December, the department shall file a report detailing its findings of the review of all certified life sciences projects that it evaluated in the prior fiscal year to the commissioner of revenue and to the joint committee on taxation and the joint committee on economic development and emerging technologies.

In bill text the following has special meaning
underline denotes added text
~~struck-out text denotes deleted text~~

2007 MA H 4234
AUTHOR: Office of the Governor
VERSION: Introduced
VERSION DATE: 09/06/2007

HOUSE No. 4234

THE COMMONWEALTH OF MASSACHUSETTS

In the Year Two Thousand and Seven.

AN ACT PROVIDING FOR THE INVESTMENT IN AND EXPANSION OF THE LIFE SCIENCES INDUSTRY IN THE COMMONWEALTH.

Whereas, The deferred operation of this act would tend to defeat its purpose, which is to provide forthwith for the immediate capital improvement needs of the commonwealth, therefore it is hereby declared to be an emergency law, necessary for the immediate preservation of the public convenience.

Be it enacted by the Senate and House of Representatives in General Court assembled, and by the authority of the same, as follows:

SECTION 1. The general court finds and declares that:

(1) promoting the economic viability and public health of the commonwealth are fundamental purposes of state government;

(2) it is imperative for the purposes of the commonwealth's economic competitiveness that the commonwealth make the investment in life sciences research, manufacturing **and commercialization** a priority to leverage revenues and to encourage collaboration and innovation among public and private institutions involved in life sciences research and related applications;

(3) further investment in the life sciences sector will also lead to new cures and treatments which may benefit all of society;

(4) the investments of the life sciences sector are intended to support Massachusetts's global leadership in life sciences-related research, innovations, commercialization, manufacturing and employment; and

(5) the purpose of this chapter is to establish a comprehensive life sciences program for the commonwealth, which would both support and stimulate research, manufacturing, **and commercialization** in this sector.

SECTION 2. To provide for a program of capital improvements to be undertaken by the Massachusetts Life Sciences Center established under chapter 23I, the sum set forth in section 3 of this act, for the several purposes and subject to the conditions specified in this act, is hereby made available, subject to the laws regulating the disbursement of public funds, which sum is in addition to any other amounts previously appropriated for these purposes.

SECTION 3.

EXECUTIVE OFFICE FOR ADMINISTRATION AND FINANCE

Massachusetts Life Sciences Center

7007-9037 For capital projects to be undertaken by the Life Sciences Center, including the preparation of plans and specifications, acquisition, construction, renovation, reconstruction, alteration, improvement, demolition, expansion and repair, of land and facilities, and for the acquisition of furnishings and equipment, all as the Life Sciences Center shall determine, for the purpose of carrying out any of its purposes set forth in chapter 23I $500,000,000

SECTION 4. To meet the expenditures necessary in carrying out section 3 of this act, the state treasurer shall, upon request of the governor, issue and sell bonds of the commonwealth in an amount to be specified by the governor from time to time but not exceeding, in the aggregate, $500,000,000. All bonds issued by the commonwealth as aforesaid shall be designated on their face, Life Sciences Center Capital Improvement Loan Act of 2007, and shall be issued for a maximum term of years, not exceeding 30 years, as the governor may recommend to the general court under section 3 of Article LXII of the Amendments to the Constitution. All such bonds shall be payable not later than June 30, 2042. All interest and payments on account of principal on these obligations shall be payable from the General Fund. Bonds and interest thereon issued under this section shall be general obligations of the commonwealth.

SECTION 5. In carrying out section 3 of this act, in addition to its powers under chapter 23I, the Massachusetts Life Sciences Center may enter into such contracts or agreements as the Center may determine to be necessary or desirable to carry out its purposes under chapter 23I and section 2 of this act with other state, local or regional public agencies or authorities, and such agencies and authorities are hereby authorized to enter into any such contracts or agreements with the Center as may be necessary or desirable to permit the Center to carry out its purposes under chapter 23I and section 3 of this act. The agreements may relate to such matters as the Center shall determine including, without limitation, the acquisition of real and personal property or any interest therein, and the design, layout, construction, reconstruction or management of construction of all or any portion of such projects. In relation to any such agreements

between the Center and other state agencies or authorities, the Center may advance monies to the agencies or authorities, without prior expenditure by the agencies or authorities, and the agencies and authorities may accept monies necessary to carry out such agreements; provided, however, that (i) the Center shall certify to the comptroller the amounts so advanced; (ii) such agreements shall contain provisions satisfactory to the Center for the accounting of such monies as expended by the agency or authority; and (iii) all monies not expended under any such agreement shall be credited to the account of the Center from which they were advanced.

SECTION 6. Notwithstanding any general or special law to the contrary, 10 days after the effective date of this act, the comptroller shall make a one-time transfer of $15,000,000 from the General Fund to the Massachusetts Life Sciences Investment Fund as established in section 5 of chapter 23I of the General Laws. The transfer shall be effective June 30, 2007.

SECTION 7. Chapter 23A of the General Laws is hereby amended by adding after section 62 the following section:-

Section 63. Massachusetts Life Sciences Sector Incentive Program

(a) Definitions.

As used in section 63, the following words shall, unless the context clearly requires otherwise, have the following meanings:

"Affiliate", any business which directly or indirectly controls or is controlled by or is under direct or indirect common control with another business, including, but without limitation, any business with whom a business is merged or consolidated, or which purchases all or substantially all of the assets of a business.

"Business", a business corporation, partnership, firm, unincorporated association or other entity engaging or proposing to engage in economic activity within the commonwealth, and any affiliate thereof, which is, or the members of which are, subject to taxation under chapter 62 or chapter 63.

"Business incubator", a facility which: (i) provides small units of space, shared support services, or financing and management assistance to new and established businesses; or (ii) is created and operated for the principal purpose of addressing conditions of unemployment and economic distress by encouraging the creation of new businesses and improving their ability to survive and grow.

"Certified life sciences project", a project that has been approved by the secretary of housing and economic development for participation in the life sciences sector incentive program pursuant to the provisions of this section.

"Commercial", non research, non development and non manufacturing related functions, including but not limited to, sales, marketing, customer support, distribution, business development, general and administrative or support functions.

"Control", the power to direct the management and policies of a business or a facility thereof, directly or indirectly, through the exercise of voting rights, by contract, or otherwise.

"Facility", the physical location, in real property owned or leased by a life sciences sector business, of a commercial or industrial activity, division or component controlled by a life sciences sector business, or any real estate project which involves the construction or renovation of real property to serve such purpose, or any combination of the foregoing, at which are employed, or are projected to be employed, permanent full-time employees of a life sciences sector business.

"Qualified US Life Science Headquarters", an affiliated group, as defined in Section 1504(a) of the Internal Revenue Code of 1986 that derives at least 70 percent of its revenue from the sale or license of life science products or intellectual property, or the rendering of contract life sciences services, or the combination of the two, if either (1) greater than 70 percent of all commercial employees, excluding sales representatives, are Massachusetts based employees, or (2) if greater than 70 percent of all tangible property (excluding inventory), leased or owned, would be apportionable to Massachusetts in the fiscal year, not withstanding the company's ability to qualify for single sales factor apportionment.

"Life sciences", advanced and applied sciences, including but not limited to, regenerative medicine, biotechnology, biopharmaceuticals, **pharmaceuticals**, nanotechnology, and medical devices.

"Life sciences sector business," a life sciences business located in the commonwealth and engaged in research, development or manufacturing, **or as a Qualified US Life Science Headquarters Company.**

"Life sciences sector incentive program" or "LSSIP", a program designed to promote increased life sciences sector development and expansion in the commonwealth, to be administered by the department of business development.

"Life sciences project", that portion of a life sciences sector business consisting of a new or expanded facility that in its entirety, as of the project proposal date, is located in the commonwealth and that:

(i) increases the number of permanent full-time employees employed by the life sciences sector business within the commonwealth; and

(ii) is not a replacement or relocation of permanent full-time employees employed by

the life sciences sector business at any other facility located within the commonwealth; and provided that in the case of a facility to be located within the commonwealth after the project proposal date, the term "project" shall refer only to a facility which is: (1) the first facility of the life sciences sector business to be located within the commonwealth; or (2) a new facility of such business and not a replacement or relocation of an existing facility of such life sciences sector business located within the commonwealth or expansion of an existing facility of the life sciences sector business which results in an increase in permanent full-time employees.

"Municipality", a city or town in the commonwealth or, in a case in which 2 or more cities or towns agree to act jointly for some purpose hereunder then, collectively, all cities and towns participating in such a collaborative agreement.

"Permanent full-time employee", an individual who: (i) at the inception of the employment relationship does not have a termination date which is either a date certain or determined with reference to the completion of some specified scope of work; (ii) works no fewer than a minimum number of weekly hours as may be specified by the department by rule or regulation and (iii) receives employee benefits at least equal to those provided to other full-time employees of the life sciences sector business. The term "increase in the number of permanent full-time employees of the life sciences sector business employed by and at the project" shall be determined with reference to this definition.

"Project proposal", a proposal submitted by a life sciences sector business to the department of business development pursuant to section 63 for designation of a project as a certified life sciences project that meets the following requirements: (i) the proposal is submitted in a timely manner as determined by the department, in such form and with such information as is prescribed by the department, supported by independently verifiable information and signed under the penalties of perjury by a person authorized to bind the life sciences sector business; (ii) the proposal includes specific targets by year of the number of additional or retained full time employees, the projected salaries for those employees, and the projected taxes generated pursuant to chapter 62 by those full time employees for each of the years for which the project may receive benefits pursuant to chapters 62, 63, or 64H; (iii) in the case of a project which as of the project proposal date is already located in the commonwealth, such projected increase shall not be less than 25 percent over the subsequent 5-year period; and (iv) in the case of a project which is a new facility within the meaning of clause (ii) of the definition of life sciences project, such proposal shall include, in addition, the number of permanent full-time employees employed by the life sciences sector business at other facilities located in the commonwealth.

"Project proposal date", the date on which a project proposal is received by the department.

"Real estate project", real property which, at a specified date subsequent to the project proposal date, there shall be initiated construction or renovation activity which, when completed, will result in an increase in the assessed value of such real property of at least

100 percent over the assessed value of such real property as of the project proposal date; provided, however, that in the case of a real estate facility which is a business incubator facility and which is designated to be a certified life sciences project pursuant to section 63, each business which executes a binding lease for space in such incubator facility subsequent to the date at which the construction or renovation activity begins shall be eligible for designation in its own right as a certified life sciences project pursuant to section 63.

"Return on investment," the tax pursuant to chapter 62 generated by permanent full-time employees of a life sciences project, which are either new or maintained because of a project, over the period for which project benefits are received.

(b) Powers and Duties.

(1) The department shall administer the life sciences sector incentive program and, in so doing, shall be empowered to exercise the following powers and duties:

(i) promulgate rules and regulations and prescribe procedures to effectuate the purposes of section 63;

(ii) review applications from life sciences sector businesses;

(iii) certify projects for participation in the life sciences sector incentive program and establish regulations for evaluating the proposals of such projects;

(iv) assist life sciences sector businesses in obtaining state and federal resources and assistance for such businesses within the commonwealth;

(v) provide appropriate coordination with other state programs, agencies, authorities, and public instrumentalities to enable activity within the life sciences sector to be more effectively promoted by the commonwealth;

(vi) monitor the implementation and operation of the life sciences sector incentive program; and

(vii) conduct a continual evaluation of the projects certified for participation in the life sciences sector incentive program.

(2) The director of the Massachusetts Life Sciences Center shall designate a staff person who shall serve as a liaison to the department and who shall regularly consult with the director of the department of business development and coordinate the efforts of the Center and department to further the purpose of this act.

(3) The department shall annually submit to the governor, the senate and the house ways and means committees, and the joint committee on economic development and emerging technologies, within 90 days after the end of its fiscal year, a complete report

detailing all projects certified under the LSSIP.

(4) Two years after the project is certified as a LSSIP, and every 2 years thereafter, the department shall prepare a report which evaluates the relative effectiveness of the LSSIP, and shall make recommendations to the secretary of housing and economic development as necessary or advisable to improve such effectiveness. Each such report shall be made available to the senate and house ways and means committees and to the joint committee on economic development and emerging technologies.

(c) Certified life sciences projects; proposals.

(1) The department may from time to time designate 1 or more projects as certified life sciences projects, and take any and all actions necessary or appropriate thereto, upon completion of the following:

(i) receipt by the department of a project proposal requesting such designation from the life sciences sector business, which includes the following:

(A) a workable plan, with precise goals and objectives, by which the life sciences sector business proposes to achieve the return on investment, that is projected, including an estimate for every year of the number of permanent fulltime employees retained or added, the average salaries of those employees, the projected taxable income pursuant to chapter 62 generated by those employees, the year the business expects to add or retain the employees, and the method by which the business shall employ aggressive affirmative action goals, objectives and identification and recruitment techniques to attain new employees;

(B) documentation regarding an agreement, if any, between the life sciences sector business and area banking institutions by which the life sciences sector business agrees to establish 1 or more accounts in such banks and such banks agree to commit a specified percentage of the funds deposited in the accounts for loans made thereby to businesses pursuant to the Massachusetts capital access program established pursuant to section 57 of chapter 23A;

(C) if appropriate, documentation in the proposal that the project is a certified economic development incentive program project, pursuant to section 3F of chapter 23A;

(D) request for a designation of the project as a certified life sciences project for a specified number of years, which shall be not less than 5 years nor more than: (i) 20 or (ii) the number of years remaining on the duration of the designation of the project as a certified economic development incentive program project, pursuant to section 3F of chapter 23A, whichever is less; and

(ii) findings made by the department, based on the project proposal, documents submitted therewith, and such additional investigation as the department shall make, and incorporate in its approval, that:

(A) the project proposal complies with the definition, all other applicable statutory requirements, and such other criteria that the department may prescribe from time to time; and

(B) the project as described in the proposal, will, if certified, achieve a projected return on investment, as specified, over the period for which it receives benefits as a certified project.

(2) A certified life sciences project shall retain its certification for the period specified by the department in its certification decision, unless such certification is revoked prior to the expiration of such specified period; provided, however, that such specified period shall be not less than 5 years (unless earlier revoked) from the date of certification nor more than: (i) 20 years from such date; or (ii) the number of years remaining on the duration of designation of the project as a certified project, including any renewals thereof, whichever is less. The department shall determine each year, beginning with the year after a project receives certification and for every year for which the project receives benefits, whether the project has satisfactorily met the specific targets by year of the number of additional or retained full time employees, the projected salaries for those employees, and the projected taxes generated pursuant to chapter 62 by those full time employees.

The certification of a project may be revoked only by the secretary of housing and economic development after an independent investigation and determination that representations made by the life sciences sector business in its project proposal are materially at variance with the conduct of the life sciences sector business subsequent to the certification; provided, however, that the department of business development shall review such certified life sciences project at least once every year; provided, further, that where the actual return on investment is less than 70 percent of the return on investment projected in the project proposal, then this shall be deemed a material variance for the purposes of a revocation determination.

A notice of decertification shall specify the date on which the decertification is effective, which may be the date of such notice or any earlier date on which the secretary of housing and economic development determines that the material variance commenced. In the event of such decertification, the commissioner of revenue shall, as of the effective date of the decertification, disallow any credits, exemptions or other tax benefits as may have been allowed by the original certification of tax benefits pursuant to this section. In addition, any credits allowed pursuant to the certification under this section shall be recaptured in a manner similar to that provided under section 31A of chapter 63 as would apply when property is disposed of or ceased to be in qualified use before the end of its useful life or, if applicable, before the end of the year in which the credit is to be taken. In the event that the original certification allowed sales and use tax exemptions under subsection 6(s) of chapter 64H, the purchaser shall accrue use tax as of the date of the decertification on a portion of the sales price on which exemption was claimed that is proportionate to the remaining useful life of the property. Nothing in this section shall

limit any other legal remedies available to the commonwealth against the life sciences sector business. Annually, on or before the first Wednesday in December, the department shall file a report detailing its findings of the review of all certified life sciences projects that it evaluated in the prior fiscal year to the commissioner of revenue and to the joint committee on taxation and the joint committee on economic development and emerging technologies.

(3) The department shall evaluate and either grant or deny any project proposal within 90 days of its project proposal date.

(d) Eligibility for tax benefits.

A certified life sciences project may be eligible for 1 or more of the tax benefits made available to life sciences projects under chapter 62, chapter 63 and chapter 64H only to the extent specified in a certification from the secretary of housing and economic development and the secretary of administration and finance. These tax benefits shall not be available to any certified life sciences project unless expressly granted by the secretaries in writing. The department of business development shall estimate in writing the tax cost of extending 1 or more benefits to a proposed project before certification, as approved in writing by the commissioner of revenue, based on reasonable projections of project activities and costs.

SECTION 8. Section 3 of chapter 23I of the General Laws is hereby amended by striking out subsection (b) and inserting in place thereof the following subsection:-

(b) The Center shall be governed and its corporate powers exercised by a board of directors consisting of the secretary of administration and finance or her designee; the secretary of housing and economic development or his designee; the president of the University of Massachusetts or his designee; 4 members who shall be appointed by the governor, 1 of whom shall be a physician licensed to practice medicine in the commonwealth and affiliated with an academic medical center, 1 of whom shall be a chief executive officer of a Massachusetts based life sciences corporation which is a member of the Massachusetts Biotechnology Council, 1 of whom shall be a researcher involved in the commercialization of biotechnology, pharmaceuticals or medical diagnostic products and 1 of whom shall be a venture capitalist, with significant experience in the life sciences sector. Each appointed member shall serve a term of 5 years. The secretary of housing and economic development shall serve as chair of the board. Any person appointed to fill a vacancy in the office of a member of the board shall be appointed in a like manner and shall serve for only the unexpired term of such member. Any member shall be eligible for reappointment. Any member may be removed from his appointment by the governor for cause.

The terms of all members appointed to the board of directors of the Life Sciences Center in 2006 under the auspices of chapter 123 of the acts of 2006 shall be terminated upon the effective date of this act. All such appointed board members terminated herein shall be eligible to be reappointed by the governor.

SECTION 9. Subsection (c) of section 3 of chapter 23I is hereby amended by striking out at the beginning of the first sentence the word "Three" and inserting in place thereof the following word:- "Four".

SECTION 10. Subsection (a) of section 4 of chapter 23I is hereby amended by adding after paragraph (29) the following paragraph:-

(30) to conduct a planning process for the implementation of the Life Sciences Center Capital Improvement Loan Act of 2007.

SECTION 11. Subsection (b) of section 5 of chapter 23I is hereby amended by striking out at the end of clause (2) the words "; provided, however, that said administrative and operational expenses shall not exceed 15 per cent of the total assets of the fund in any one fiscal year;"

SECTION 12. Section 5 of chapter 23I is hereby amended by striking out subsection (c) and inserting in place thereof the following subsection:-

(c) The fund shall be held and applied by the Center, subject to the approval of the board, to make qualified investments, grants, research and other funding, and loans, designed to advance the following public purposes: (1) to stimulate increased financing for the expansion of research and development in the areas of life sciences, nano-technology, biotechnology and stem cell research in the commonwealth by leveraging private financing for highly productive state-of-the-art research and development facilities, equipment and instrumentation and by providing financing related thereto including, without limitation, financing of the construction or expansion of such new facilities; (2) to make targeted investments, including research funding, and funding for the development of devices and drugs, in the areas of life sciences, nanotechnology, biotechnology and stem cell research and to spur manufacturing activities for new or existing advanced technologies and life sciences in the commonwealth; (3) to make matching grants to universities, colleges, public instrumentalities, companies and other entities to induce the federal government, industry and other grant-funding sources to fund the expansion of research and development in the areas of life sciences, nano-technology, biotechnology and stem cell research in the commonwealth, and to thereby serve to increase and strengthen the commercial and industrial base of the commonwealth and the economic development and employment opportunities related thereto; (4) to provide bridge financing to universities, colleges, public instrumentalities, companies and other entities in anticipation of the receipt of grants of the type described in clause (2) awarded or to be awarded by the federal government, industry or other sources; (5) to provide fellowships and grants; (6) to provide work force training grants to prepare individuals for life sciences careers; and (7) to otherwise further the public purposes set forth in this act.

SECTION 13. Section 5 of chapter 23I is hereby amended by adding the following subsection:-

(h) The Life Sciences Center and the board shall be advised by a 10- member advisory committee, whose members shall consist of individuals appointed by the governor and who are active members of the Massachusetts Life Sciences Collaborative, or any successor organization thereto. Half of the members shall initially serve for a term of 3 years and half of the members shall serve for a term of 4 years. Each member, thereafter, shall serve for a term of 3 years. Any person appointed to fill a vacancy in the office of a member of the committee shall be appointed in a like manner and shall serve for only the unexpired term of such member. Any member shall be eligible for reappointment. Any member may be removed from his appointment by the governor for cause. The members of the committee shall serve without compensation, but each member shall be entitled to reimbursement for his actual and necessary expenses incurred in the performance of his or her official duties. The duties of the advisory board shall be to advise concerning issues related to: research in the life sciences; development of products and the efficacy of the public and private initiatives to further product development in the life sciences; commercialization of biotechnology, pharmaceuticals, medical diagnostic products or such other areas within the life sciences; and any other such area as is requested by the board of the Life Sciences Center.

The advisory committee shall not be a state agency for the purposes of chapter 268A and shall not be subject to section 11A 1/2 of chapter 30A or chapter 66.

SECTION 14. Section 6 of chapter 62 of the General Laws is hereby amended by adding after subsection (l) the following subsection:-

(m) Life Sciences Investment Incentive Tax Credit

(1) A taxpayer subject to tax under this chapter, which operates a certified life sciences project as defined in section 63 of chapter 23A, may take a credit against the taxes imposed by this chapter, to the extent provided in a certification pursuant to section 63 of chapter 23A, in an amount equal to 10 percent of the cost of qualifying property used exclusively in the commonwealth in such project. Qualifying property shall be tangible personal property and other tangible property including buildings and structural components of buildings acquired by purchase, as defined under Section 179(d) of the Code, as amended and in effect for the taxable year, but not including property that is taxable under Chapter 60A, provided, however, that such property must be depreciable under section 167 of the Code and have a useful life of 4 years or more. If such property is disposed of or ceases to be in qualified use before the end of its useful life or before the end of the year in which the credit is to be taken, the recapture and related provisions of subsection (e) of section 31A of chapter 63 shall apply. A taxpayer taking a credit allowed under this subsection (m) may not take the credit allowed by subsection (g) except to such extent, not to exceed 2 percent of the cost of any qualifying property, as may be provided in a certification pursuant to section 63 of chapter 23A.

A credit is allowed under this section only to the extent that the taxpayer files the application with the department of business development, in a form as may be determined

by the department, within 1 year after the initial project certification pursuant to section 63 of chapter 23A.

The department may certify that property eligible for the credit is a certified life sciences project as defined in section 63 of chapter 23A, and that the certified life sciences project reasonably satisfies the return on investment projections specified in the original project proposal as defined in section 63 of chapter 23A. Based upon the information provided in the application and its own independent investigation, the department shall determine whether the certified life sciences project is in compliance with the definition of certified life sciences project and whether the project has a reasonable chance of completing the return on investment as advanced in the initial proposal as certified by the department. If the department determines that the certified life sciences project is no longer in compliance, then the secretary of housing and economic development shall revoke certification of the project as provided in section 63 of chapter 23A and shall provide notification of decertification to the commissioner of revenue. Nothing in this section shall limit the authority of the commissioner to make adjustments to a taxpayer's liability upon audit. Nothing in this section shall limit any other legal remedies available to the commissioner of revenue or the commonwealth against the life sciences sector business.

(2) Any taxpayer entitled to a credit under this section for any taxable year may carry over and apply to its tax for any 1 or more of the next succeeding 10 taxable years, the portion, as reduced from year to year, of those credits which exceed the tax for the taxable year; provided, however, that in no event shall the taxpayer apply the credit to its tax for any taxable year beginning more than 10 years after the certified life sciences project ceases to qualify as such under the provisions of chapter 23A.

(3) The commissioner of revenue shall promulgate such rules and regulations as are necessary to implement the provisions of this section. Such rules and regulations may provide the adjustment of intercompany prices and elimination of intercompany transactions to ensure that all amounts upon which the credit is based reasonably reflect fair market value. In addition, such rules and regulations shall include provisions to prevent the generation of multiple credits with respect to the same property.

(4) In the event that such credit allowed to a certified life sciences project under this subsection, or such credit as may be allowed under subsection (g) as limited in this subsection, exceeds the tax otherwise due under chapter 62, the balance of such credit shall, at the option of the taxpayer, be refundable to the taxpayer for the taxable year in which qualified property giving rise to that credit is placed in service. If such credit balance is refunded to the taxpayer, then the credit carryover provisions of paragraph (2), and of subsection (g)(2), do not apply.

SECTION 15. Section 6 of chapter 62 of the General Laws is hereby amended by adding after subsection (m), the following subsection:-

(n) Certified Life Sciences Project User Fee Credit

(1) As used in this section, the following words shall, unless the context otherwise requires, have the following meanings:

"Primarily", more than 50 percent.

"Research and development costs", in-house research expenses within the meaning of section 41(b)(2) of the Code **and, with respect to Qualified US Life Science Headquarters Companies, qualified research expenses as defined in section 41(b)of the code, to the extent they relate to legally mandated clinical trial activities not otherwise taken into account as research and development costs**.

"User fees", the monetary amount actually paid by a certified life sciences project to the U.S.F.D.A. that constitutes the fee due upon the submission of a human drug application or supplement pursuant to 21 U.S.C. Section 379h(a)(1) for a human drug, the research and development costs of which, were primarily incurred in the commonwealth, **or 100 percent of such fees if the company is a Qualified US Life Science Headquarters Company**.

"U.S.F.D.A.", the United States Food and Drug Administration.

(2) Except as otherwise limited by paragraph (e), there may be allowed to any certified life sciences project, as defined by section 63 of chapter 23A, as a refundable credit against the tax liability imposed under this chapter an amount equal to 100 percent of the cost of user fees paid by such certified life sciences project, to the extent provided in a certification pursuant to section 63 of chapter 23A.

(3) A certified life sciences project shall claim the credit in the taxable year in which its application for the licensure of an establishment to manufacture the human drug in the commonwealth is approved by the U.S.F.D.A.

(4) A credit allowed under this section may be taken only after the taxpayer completes an application signed by an authorized representative of the applicant, and files the application with the department of business development within 1 year after the initial project certification pursuant to section 63 of chapter 23A.

(5) In the event that such credit allowed to a certified life sciences project exceeds the tax otherwise due under chapter 62, the balance of that credit shall be refundable to the taxpayer for the taxable year in which the credit is claimed.

(6) The deduction from gross income that may be taken with respect to any expenditures qualifying for the credit under this section shall be disallowed to the extent of the credit.

(7) Only user fees paid by a certified life sciences project to the U.S.F.D.A. on or after the effective date of this section are eligible for the credit.

(8) To the extent a deduction is disallowed under (6) above, it shall not be disallowed more than once after consideration of the Federal Orphan Drug credit add back as set forth in section 280C(b) of the code. Furthermore, it shall be clarified that the amount of any Orphan Drug Credit addback, included in Federal taxable income under Section 280C(b), shall not be considered as taxable income for purposes of the Massachusetts taxable income base.

SECTION 16. Section 30 of chapter 63 is hereby amended by adding after paragraph 15 the following paragraph:-

(16) Notwithstanding the last sentence in paragraph (5)(b) of this section, losses sustained in any taxable year by a certified life sciences project may, to the extent provided in a certification pursuant to section 63 of chapter 23A, be carried forward for not more than 15 years and may not be carried back.

SECTION 17. Chapter 63 of the General Laws is hereby amended by adding after section 31L the following section:-

Section 31M. Certified Life Sciences Project User Fee Credit

(a) As used in this section, the following words shall, unless the context otherwise requires, have the following meanings:

"Primarily", more than 50 percent.

"Research and development costs", in-house research expenses within the meaning of section 41(b)(2) of the Code.

"User fees", the monetary amount actually paid by a certified life sciences project to the U.S.F.D.A. that constitutes the fee due upon the submission of a human drug application or supplement pursuant to 21 U.S.C. Section 379h(a)(1) for a human drug, the research and development costs of which were primarily incurred in the commonwealth.

"U.S.F.D.A.", the United States Food and Drug Administration.

(b) Except as otherwise limited by paragraph (e), there shall be allowed to any certified life sciences project, as defined by section 63 of chapter 23A, as a refundable credit against the tax liability imposed under this chapter an amount equal to 100 percent of the cost of user fees paid by such certified life sciences project, to the extent provided in a certification pursuant to section 63 of chapter 23A.

(c) A certified life sciences project shall claim the credit in the taxable year in which its application for the licensure of an establishment to manufacture the human drug in the commonwealth is approved by the U.S.F.D.A. **or the company is a Qualified US Life Science Headquarters Company for the fiscal year.**

(d) A credit allowed under this section may be taken only after the taxpayer completes an application signed by an authorized representative of the applicant, and files the application with the department of business development within 1 year after the initial project certification pursuant to section 63 of chapter 23A.

(e) The credit allowed may reduce the excise due under section 32(b), or 39(b). The credit allowed to a certified life sciences project is not subject to the provisions of section 32C. In the event that such credit allowed to a certified life sciences project exceeds the excise otherwise due under section 32(b) or section 39(b) of chapter 63, the balance of that credit shall be refundable to the taxpayer for the taxable year in which the credit is claimed.

If a certified life sciences project files as a member of a combined group and applies its excess credit against the excise of another group member, then the credit as applied to corporations other than such certified life sciences project is not subject to the provisions of section 32C and may reduce to zero the excise due under section 32(b), or 39(b) and under any act in addition thereto. In the event that such credit allowed to a certified life sciences project that is applied against the excise liability of such other corporations exceeds the excise otherwise due to such corporations under chapter 63, the balance of that credit shall be refundable to the taxpayer for the taxable year in which the credit is claimed.

(f) For purposes of section 30, the deduction from gross income that may be taken with respect to any expenditures qualifying for the credit under this section is disallowed to the extent of the credit.

(g) Only user fees paid by a certified life sciences project to the U.S.F.D.A. on or after the effective date of this section are eligible for the credit.

SECTION 18. Subsection (f) of section 38 of chapter 63 of the General Laws is hereby amended by adding after subparagraph (5) the following subparagraph:-

(6) To the extent provided in a certification pursuant to section 63 of chapter 23A, a certified life sciences project, as defined in section 63 of chapter 23A, is deemed to be *taxable in the state of the purchaser if the property of the project is manufactured in the* commonwealth and delivered or shipped to a purchaser in another state.

SECTION 19. Section 38C of chapter 63 of the General Laws is hereby amended by adding the following sentence at the end thereof:-

A certified life sciences project shall, to the extent provided in a certification pursuant to section 63 of chapter 23A, be deemed to be a research and development corporation for purposes of exemptions under chapters 64H and 64I.

SECTION 20. Section 38M of chapter 63 of the General Laws is hereby amended by

adding after subsection (i) the following subsection:-

(j) To the extent provided in a certification pursuant to section 63 of chapter 23A, in the event that the credit allowed under this section is allowed with respect to a certified life sciences project and the credit that may be claimed by a taxpayer under this section exceeds the amount that may otherwise be allowed under this section for a taxable year, the balance of that credit attributable to a certified life sciences project shall, at the option of the taxpayer and to the extent provided in such certification, be refundable to the taxpayer for the taxable year. If such credit balance is refunded to the taxpayer, then the credit carryover provisions of subsection (f) shall not apply.

SECTION 21. Chapter 63 of the General Laws is hereby amended by adding after section 38T the following section:-

Chapter 63: Section 38U. Life Sciences Investment Incentive Tax Credit

Section 38U. (a) A corporation subject to the excise imposed under this chapter, which operates a certified life sciences project as defined in section 63 of chapter 23A, may take a credit against the excise imposed by this chapter, to the extent provided in a certification pursuant to section 63 of chapter 23A, in an amount equal to 10 percent of the cost of any qualifying property used exclusively in the commonwealth in such project. Qualifying property shall be tangible personal property and other tangible property including buildings and structural components of buildings acquired by purchase, as defined under Section 179(d) of the Code, as amended and in effect for the taxable year, but not including property that is taxable under Chapter 60A, provided, however, that such property must be depreciable under section 167 of the Code and have a useful life of 4 years or more. If such property is disposed of or ceases to be in qualified use before the end of its useful life or before the end of the year in which the credit is to be taken, the recapture and related provisions of subsection (e) of section 31A of chapter 63 shall apply.

A credit is allowed under this section only to the extent that the taxpayer files the application with the department of business development, in a form as may be determined by the department, within 1 year after the initial project certification pursuant to section 63 of chapter 23A.

The credit allowed under this section may be taken by an eligible corporation; provided, however, that neither credit allowed by section 31A or section 31H is taken by such corporation; and provided further that the credit allowed by section 38N shall not be taken except to such extent, not to exceed 2 percent of the cost of any qualifying property, as may be provided in a certification pursuant to section 63 of chapter 23A.

The department may certify that property eligible for the credit is a certified life sciences project as defined in section 63 of chapter 23A, and that the certified life sciences project reasonably satisfies the return on investment projections specified in the original project proposal. Based upon the information provided in the application and its

own independent investigation, the department shall determine whether the certified life sciences project is in compliance with the definition of certified life sciences project and whether the project has a reasonable chance of completing the return on investment as advanced in the initial proposal as certified by the department. If the department determines that the certified life sciences project is no longer in compliance, then the secretary of housing and economic development shall revoke certification of the project as provided in section 63 of chapter 23A and shall provide notification of decertification to the commissioner of revenue. Nothing in this section shall limit the authority of the commissioner to make adjustments to a corporation's liability upon audit. Nothing in this section shall limit any other legal remedies available to the commissioner of revenue or the commonwealth against the life sciences sector business.

(b) The credit allowed by this section shall not be subject to the provision of section 32C.

(c) In the case of a corporation that is subject to a minimum excise under any provision of this chapter, the amount of the credit allowed by this section shall not reduce the excise to an amount less than such minimum excise.

(d) Any corporation entitled to a credit under this section for any taxable year may carry over and apply to its excise for any 1 or more of the next succeeding 10 taxable years, the portion, as reduced from year to year, of those credits which were not allowed by paragraph (c) or which exceed the excise for the taxable year; provided, however, that in no event shall the corporation apply the credit to its excise for any taxable year beginning more than 10 years after the certified life sciences project ceases to qualify as such under the provisions of chapter 23A.

(e) In the case of corporations filing a combined return of income under section 32B, a credit generated by an individual member corporation under the provisions of this section shall first be applied against the separately determined excise attributable to that member, subject to the limitations of paragraph (c). A member corporation with an excess credit may apply its excess credit against the excise of another group member, to the extent that such other member corporation can use additional credits under the limitation of paragraph (c). Unused, unexpired credits generated by member corporations shall be carried over from year to year by the individual corporation that generated the credit.

(f) The commissioner of revenue shall promulgate such rules and regulations as are necessary to implement the provisions of this section. Such rules and regulations may provide the adjustment of intercompany prices and elimination of intercompany transactions to ensure that all amounts upon which the credit is based reasonably reflect fair market value. In addition, such rules and regulations shall include provisions to prevent the generation of multiple credits with respect to the same property.

(g) In the event that such credit allowed to a certified life sciences project under this section, or such credit as may be allowed under section 38N of this chapter as limited in this subsection, exceeds the excise otherwise due under chapter 63, the balance of such

credit shall, at the option of the taxpayer, be refundable to the taxpayer for the taxable year in which qualified property giving rise to that credit is placed in service. If such credit balance is refunded to the taxpayer, then the credit carryover provisions of paragraph (d), and of section 38N of this chapter, do not apply.

SECTION 22. Section 42B of chapter 63 of the General Laws is hereby amended by adding the following sentence at the end thereof:-

A certified life sciences project shall, to the extent provided in a certification pursuant to section 63 of chapter 23A, be deemed to be a research and development corporation for purposes of exemptions under chapters 64H and 64I.

SECTION 23. Section 6 of chapter 64H of the General Laws is hereby amended by adding after subsection (ww) the following subsection:-

(xx) For purposes of this paragraph the term "utility support systems" means all areas of utility support systems including, but not limited to, site, civil, mechanical, electrical and plumbing systems.

Sales of tangible personal property purchased for a certified life sciences project, as defined by section 63 of chapter 23A,for use in connection with the construction, alteration, remodeling, repair, or remediation of the research, development or manufacturing facilities and the utility support systems provided that such facilities and utility support systems are constructed, altered remodeled, repaired or remediated in furtherance of a certified life sciences project. This section shall apply only to the extent provided in a certification pursuant to section 63 of chapter 23A.

Such purchases made on or after the effective date of this section shall only be eligible for this exemption.

SECTION 24. Section 38 of chapter 63 of the General Laws is hereby amended by adding after subsection (n) the following subsection:-

A qualified US Life Science Headquarters Company shall be eligible to use singles sales factor apportionment for any tax year ending after enactment.

SECTION 25. Section 38(c) of chapter 63 of the General Laws is hereby amended by inserting after "a manufacturing corporation as described in subsection (l)," the following phrase:

...a qualified US Life Science Headquarters Company, as described in chapter 23A of the General Laws, Section 63(a),

Section by Section Summary of
H4234
November 7, 2007

SECTION 1. Outlines the purpose of the bill.

SECTION 2. Provides for a capital improvement program to be undertaken by the MLSC.

SECTION 3. Provides $500,000,000 in capital funding, over 10 years, for capital projects undertaken by MLSC.

SECTION 4. Provides authority for the Commonwealth to sell bonds to raise funds for capital projects. Bonds will be 30-year bonds, payable not later than year 2042.

SECTION 5. Gives authority to MLSC to enter into contracts and agreements necessary to carry out bonding and capital projects.

SECTION 6. Appropriates $15m for the MLSC effective June 30, 2007.

SECTION 7. Amends Chapter 23A to create a new Life Sciences Sector Investment Program, which allows life sciences businesses to apply to the Department of Business Development for certification as a "certified life sciences project." The Secretary of Housing and Economic Development awards the certification.

Any life sciences sector business, which is defined as a life sciences business located in the Commonwealth and engaged in research, development or manufacturing, is eligible to apply for certification.

"Life sciences" is defined as: advanced and applied sciences, including but not limited to, regenerative medicine, biotechnology, biopharmaceuticals, nanotechnology, and medical devices.

A "project" is defined as that portion of a life sciences sector business consisting of a new or expanded facility in the Commonwealth. To be defined as a project, a life sciences business must increase the number of its permanent full-time employees. The employees must not be a replacement or relocation of permanent full-time employees employed by the business at any other facility located within the commonwealth.

Once certified, a project is eligible to receive one or more of 7 tax incentives created through this bill. The Secretary of Housing and Economic Development and the Secretary of Administration and Finance jointly award the tax incentives on a project by project basis (the tax incentives are outlined in further sections).

A project's certification may be revoked by the Secretary of Housing and Economic Development if the business does not meet at least 70% of its employment goals as outlined in its proposal.

SECTION 8. Amends Section 3 of Chapter 23I,[1] which created the MA Life Sciences Center, by increasing the number of gubernatorial appointments from 2 to 4 and specifies that one of the new appointees shall be a researcher and one shall be a venture capitalist. Currently there are a total of 5 board members; this would increase the total to 7 board members.

This section also provides that all current board members' appointments shall expire upon approval of the bill.

SECTION 9. Amends subsection (c) of section 3 of Chapter 23I to increase the quorum requirement from 3 to 4 to reflect the increased size of the board.

SECTION 10. Amends subsection (a) of section 4 of Chapter 23I to increase the duties and powers of the MLSC to include conducting a planning process for implementation of the capital project portions of the bill.

SECTION 11. Amends subsection (b) of section 5 of Chapter 23I to lift the 15% administrative cap for administrative and operational expenses.

SECTION 12. Amends subsection (c) of section 5 of Chapter 23I to expand the purposes of the MLSC Fund to include: providing fellowships and grants, providing for workforce training grants to prepare individuals for life sciences careers; and allowing funds to be spent in furtherance of the purposes set forth in the act.

SECTION 13. Amends section 5 of Chapter 23I to create a 10 member advisory board for the MLSC. The board shall consist of individuals appointed by the Governor who are active members of the MA Life Sciences Collaborative. The terms of the appointees are staggered; half serve initially for 3 years and half initially serve for 4 years. The members serve without compensation. Their duties shall be to advise concerning issues related to: research in the life sciences; development of products and the efficacy of the public and private initiatives to further product development in the life sciences; commercialization of biotechnology, pharmaceuticals, medical diagnostic products or such other area within the life sciences; and any other such area as is requested by the board of the Life Sciences Center.

NOTE ON SECTIONS FOLLOWING: The remaining sections provide for tax credits and incentives to certified life sciences projects. There are 3 tax credits outlined first and each may be taken both by individuals and by corporations, therefore, there is corresponding language for each tax credit in Chapter 62, which outlines credits for individuals and Chapter 63, which outlines tax credits for corporations. For ease of reading, the sections in this summary are grouped together by tax credit. Sections 16, 18, 19, 22 and 23 outline 4 tax incentives.

SECTIONS 14 and 21. Create a Life Sciences Investment Incentive Tax Credit. Section 14 amends Section 6 of chapter 62; Section 20 of the bill amends Section 63 by adding a new section 38U. The Life Sciences Investment Incentive Tax Credit is a 10% refundable tax credit

[1] Chapter 23I is the enabling statute for the Massachusetts Life Science Center; it appears in Section 24 of Chapter 123 of the Acts of 2006, the Economic Stimulus Package.

Summary of Draft Life Sciences Package

July 18, 2007

1. **Funding for Life Sciences Initiative**

   - Provides $500m in capital funding.
   - Appropriates $15m for the Mass. Life Sciences Investment Fund.

2. **Increasing the Number of Governor Appointees to the MLSC Board from 2 to 4, Creating an Advisory Board and Lifting the Cap on MLS Admin Funds**

   - Increases the number of Governor Appointees from 2 to 4 and requires that the additional 2 appointees be a venture capitalist and a researcher.
   - Secretary of Housing and Economic Development to serve as chair.
   - Reconstitutes the present membership of the board.
   - Changes the quorum quota for board meetings from 3 to 4.
   - Mandates a capital planning process to implement the capital provisions of the proposal.
   - Lifts the administrative cap for MLSC.
   - Increases the fund allowable activities so that MLSC has the authority to build capital projects, award grants, and expend funds consistent with the plan articulated by the Governor.
   - Establishes a 10 person advisory committee to the MLSC from members of the Massachusetts Life Sciences Collaborative.

3. **Expansion of Tax Code Provisions for Life Sciences Companies**

   - Creates a new Life Sciences Sector Investment Program (necessary to set up the tax incentive piece) which requires life sciences businesses to become "certified life sciences projects" to be eligible to receive tax benefits. Any research or manufacturing business, both corporations and non-corporate entities, can apply to be certified. The Department of Business Development is responsible for administering the program and certifying projects; the Secretary of HED and Secretary of ANF jointly award the tax incentives.
   - Certification will be predicated upon the projected return on investment for the project from the taxable income generated by the project's new, permanent full-time employees.

- Creates tax incentives for certified life sciences sector projects.

  - a. Eliminates the MA throwback provision;
  - b. Creates a redeemable 10% 10 year carry forward Life Sciences Investment Incentive Tax Credit and allows projects to receive an additional 2% tax credit if they locate in Economic Opportunity Areas.
  - c. Creates a sales tax pass through for bricks and mortar purchased associated with the development of life sciences projects;
  - d. Creates a 100% refundable FDA User Fee Credit;
  - e. Allows a life sciences project to take the current Research and Development Tax Credit as a refundable credit;
  - f. Extends the NOL (Net Operating Loss Credit) to 15 years;
  - g. Eliminates the mathematical test so that true R&D companies can take sales and use tax exemption on appropriate purchases with certainty, as manufacturers do.

- Imposes a yearly project evaluation and provides for project decertification in the event that a company fails to achieve the projected return on investment mandated as part of the project certification.