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BILL ANALYSIS

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Senate Bill 568 (Substitute S-2)
Sponsor: Senator Wayne Kuipers
Committee: Economic Development and Regulatory Reform

Date Completed: 1-23-08

CONTENT

The bill would amend the Income Tax Act to reduce the minimum amount of a taxpayer's initial equity investment in a "qualified business" from $100,000 to $25,000, in order for the taxpayer to take a deduction for a gain realized from the investment. The bill also would extend the deadline for making the investment.

Under the Act, for tax years beginning after December 31, 2006, a taxpayer may deduct, to the extent included in adjusted gross income, all or a portion of the gain realized from an initial equity investment of at least $100,000 made by the taxpayer before December 31, 2009, in a qualified business, if an amount equal to the sum of the taxpayer's basis in the investment plus the gain, or a portion of that amount, is reinvested in an equity investment in a qualified business within one year after the sale or disposition of the investment in the qualified business. Under the bill, the deduction would be allowed if the minimum initial equity investment were $25,000, rather than $100,000, and were made by December 31, 2011.

"Qualified business" means a business that complies with all of the following:

-- Is a seed or early stage business as defined in the Michigan Early Stage Venture Investment Act.
-- Has its headquarters, is domiciled, or has a majority of its employees working a majority of their time in Michigan.
-- Has a preinvestment valuation of less than $10 million.
-- Has existed less than five years.
-- Is engaged only in competitive edge technology.
-- Is certified by the Michigan Strategic Fund as meeting these requirements at the time of each proposed investment.

(The requirement that a qualified business have been in existence less than five years does not apply to a business whose business activity is derived from research at an institution of higher education located in Michigan or an organization that is exempt from Federal taxes under Section 501(c)(3) of the Internal Revenue Code and is located in Michigan.)

MCL 206.30 Legislative Analyst: Patrick Affholter

FISCAL IMPACT

The fiscal impact cannot be identified because of many unknown variables. In fact, it is still not possible to estimate the fiscal impact of the existing deduction because: 1) the first year the current deduction may be claimed is the 2007 tax year and no information is yet available on how many taxpayers will claim this deduction or how much will be deducted, and 2) there is no way to estimate the amount of capital gains investors will realize from initial equity investments, how much of these initial investments and subsequent gains will be reinvested in qualified businesses, or when these gains will be realized and reinvested. Given that the fiscal impact of the existing deduction is not known, it is not possible to provide a reasonable estimate of the fiscal impact of the change to the current deduction proposed in this bill. All that is known at this time is that the cost of the deduction would increase under this bill because the minimum amount of the initial equity investment needed to qualify for the deduction would be lowered from $100,000 to $25,000 and, therefore, more taxpayers would qualify for the deduction. This bill would have no direct fiscal impact on local government.

Fiscal Analyst: Jay Wortley