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BILL ANALYSIS

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Senate Bill 576 (as introduced 6-7-07)
Sponsor: Senator Hansen Clarke
Committee: Economic Development and Regulatory Reform

Date Completed: 11-28-07

CONTENT

The bill would amend the Income Tax Act to revise a tax deduction for a gain realized from a taxpayer's initial equity investment in a "qualified business", by reducing the required minimum investment from $100,000 to a $25,000 share of a total investment of at least $100,000, subject to reinvestment requirements.

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 for all or a portion of the gain realized from a total initial equity investment of at least $100,000, if the taxpayer's share of the total initial investment were at least $25,000 and if an amount equal to the sum of the taxpayer's basis in the investment plus the gain, or a portion of that amount, were reinvested in a total equity investment of at least $100,000 in a qualified business within one year after the sale or disposition of the investment in the qualified business.

"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 it would lower the minimum amount of a taxpayer's share of the initial equity investment needed to qualify for the deduction and, therefore, more taxpayers would qualify for the deduction. This bill would have no direct fiscal impact on local governments.

Fiscal Analyst: Jay Wortley

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