Testimony Presented to the
Commerce Committee of the Connecticut General Assembly

Tuesday, March 12, 2019

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S.B. 1026 An Act Establishing Certain Incentives to Grow the Bioscience Industry in the State
H.B. 5005 An Act Extending the Angel Investor Tax Credit and Expanding Eligibility for the State's Set-Aside Program for Small Contractors

Good morning Senator Hartley, Representative Simmons, Senator Cohen, Representative Elliott, Senator Martin, Representative Cummings, members of the Commerce Committee.

I'm Paul Pescatello, Senior Counsel and Executive Director of the Connecticut Bioscience Growth Council.

I am also President/CEO of the New England Biotechnology Association and Chair of We Work for Health Connecticut.

The Connecticut Bioscience Growth Council is a committee of the Connecticut Business and Industry Association's biotech and biopharma members.

The Bioscience Growth Council was formed as a means to foster collaboration both among Connecticut biotech and biopharma companies themselves and, just as importantly, *with* our state. As you know, Connecticut – *this* General Assembly – has chosen wisely to invest in the life sciences as a foundation for Connecticut's 21st century economy and as a means to create a broad spectrum of jobs.

I am here today to speak in support of S.B. 1026, An Act Establishing Certain Incentives to Grow the Bioscience Industry in the State.

Connecticut has made significant investments in the life sciences both to help fund treatments and cures for patients and to encourage the growth of the biopharma industry. The economic development value of biopharma is significant:

- the sector spends in excess of $55 billion per year on research and development, creating jobs with an average salary of $95,000 per year, which is 85% greater than the overall private sector average.
- every new job in the industry results in an additional 3.9 jobs created.
- Connecticut ranks 4th in the nation for bioscience patents per 1,000 people.
- 54% of all venture capital invested in Connecticut is in bioscience.
- 80% of all Connecticut academic research and development investments are in bioscience.
- Connecticut's bioscience sector currently employs nearly 39,000 workers in over 2,500 companies.

Because of Connecticut biopharma's robust economic impact and the state's need for economic growth and high value-added/high paying job creation, S.B. 1026 is especially important. The bill targets key issues that, addressed through this legislation, will lessen barriers to further growth.

S.B. 1026 eliminates the capital stock tax which disproportionately affects early-stage biopharma companies. It is essentially a tax on hard-earned research and development savings accounts. I attach to this testimony, my testimony on H.B. 5261, An Act Phasing Out the Capital Stock Tax, and H.B. 6459, An Act Concerning the Capital Base Tax, heard last week before the Finance, Revenue and Bonding Committee, each of which has a similar goal of eliminating the capital base tax.

S.B. 1026 would also restore Connecticut's research and development tax credits to 100% of their value. This is a critical measure necessary to achieve our goal of harvesting the dividends promised by Connecticut's investment in the life sciences – the good jobs and the powerful and hugely positive ripple effect of private sector biopharma investment across the Connecticut economy. Recognizing the importance of research and development is critical. Getting research and development policy "right" is key.

More than any other industry, the life sciences and biopharma companies are defined by research and development.

It takes about 12 years and $2.7 billion to bring a new medicine from concept to the finish line of an FDA approved product available on pharmacy shelves. It is important to understand that most projects are discarded along the research and development pathway. Most great research leads to new insights and further research, but only rarely does it lead to new medicines. Conservatively estimated, something on the order of only 1 out of 1,000 research projects become an FDA approved medicine. Nevertheless, the state where all this research occurs obtains the benefit of all the research investment dollars being circulated throughout its economy, whether that research results in profitable new medicines, or not.

Since biopharma is about research and development it is not difficult to see that scientists and entrepreneurs and investors – existing and start-up companies/employers – choose where to do their research and development, where to set up their essential operations, in states that recognize the value of all that comes with the commitments and risks inherent in huge research and development spends.

For state government the means to recognize the value of research and development spending is through the tax code.

The incentive is: do your research and development here, make your vast research and development investments here, take your risks here and we will give you a credit against *future* income.

The bargain is, the benefit to the state is, we get the benefit *now* of all those investment dollars infused in our economy, we receive all the income and property and sales taxes paid by biopharma employees for a credit against *future* income.

It cannot be underscored boldly enough: research and development tax credits are earned by companies only *after* they've made an investment, *after* they've spent funds in Connecticut.

What have we done in Connecticut? We've created a set of research and development tax credits that are competitive with other states that attract biopharma companies. But then we have hobbled the effectiveness of this policy by adding limitations to how much income a company can offset with the research and development tax credits they have earned. S.B. 1026 fixes this flaw.

S.B. 2016 represents a comprehensive plan, with provision for future CTNext funding, funding for Connecticut Innovations to contract with an advertising agency to create a marketing plan, social media campaign and improved biopharma website, and to establish a "one stop shopping" "biotechnology ambassador" at the Department of Economic and Community Development.

I would like now to turn to H.B. 5005, An Act Extending the Angel Investor Tax Credit Program and Expanding Eligibility for the State's Set-Aside Program for Small Contractors.

It is important to bear in mind that two primary factors determine how and where life sciences research and development and biopharma companies will locate. First, the quality of the basic life sciences research of local research institutions and universities.

Simply put, life sciences researchers, entrepreneurs and, especially, biopharma company founders need to be close to the research labs and colleagues that were integral to the core research findings that led them to see commercial potential and start a new research project and/or for-profit enterprise.

We are fortunate in Connecticut to have several leading life sciences research institutions. The quality and quantity of research grants and projects ongoing at Yale University, University of Connecticut and at many other Connecticut colleges and universities provides us with many opportunities to root new biotech ventures in Connecticut. Bringing The Jackson Laboratory to Connecticut was wise economic development policy because it grew the size and quality of Connecticut's portfolio of cutting-edge life sciences research.

But there is only so much state policymakers can do to boost academic research.

The second determining factor of where a biotech venture will start operating, and almost as important as proximity to academic research, is access to capital. This makes the angel investor tax credit one of the *most* effective incentives we have to boost the growth of the Connecticut biopharma sector.

I urge you to vote in favor of S.B. 1026 and H.B. 5005.

I would be happy to answer any questions you may have or expand upon any points made in my testimony.

Thank you.

Testimony Presented to the Finance, Revenue and Bonding Committee of the Connecticut General Assembly

Monday, March 4, 2019

Paul R. Pescatello, JD, PhD

H.B. 5261 An Act Phasing Out the Capital Stock Tax
H.B. 6459 An Act Concerning the Capital Base Tax

Good afternoon Senator Fonfara, Representative Rojas, Senator Witkos, Representative Davis, Senator Cassano, Senator Leone, Representative Concepcion, Representative Meskers, members of the Finance, Revenue and Bonding Committee.

I'm Paul Pescatello, Senior Counsel and Executive Director of the Connecticut Bioscience Growth Council.

I am also President/CEO of the New England Biotechnology Association and Chair of We Work for Health Connecticut.

The Connecticut Bioscience Growth Council is a committee of the Connecticut Business and Industry Association's biotech and biopharma members.

The Bioscience Growth Council was formed as a means to foster collaboration both among Connecticut biotech and biopharma companies themselves and, just as importantly, *with* our state. As you know, Connecticut – *this* General Assembly – has chosen wisely to invest in the life sciences as a foundation for Connecticut's 21st century economy and as a means to create a broad spectrum of jobs.

I am here today to speak in support of elimination of the capital stock tax. Two bills before you, H.B. 5261, An Act Phasing Out the Capital Stock Tax and H.B. 6459, An Act Concerning the Capital Base Tax, have elimination of this tax as their goal.

Currently, corporations are taxed by the State of Connecticut pursuant to a three-part test. Corporations pay the greater of: (1) $250; (2) a levy on income, with the 7.5% statutory rate subject to a 20% surcharge, making the top Connecticut marginal corporate tax rate 9%; or (3) a .31% tax on the "capital base."

The capital base tax works as a powerful *dis*incentive to formation of start-up enterprises in Connecticut and encourages entrepreneurial activity to occur outside Connecticut's borders.

Because the capital base tax is essentially a tax on corporate retained earnings, which of course includes *savings* of all kinds, such as funds raised by new ventures from investors, it especially works as a deterrent to the formation and growth of enterprises which need to raise and hold large sums for research and development.

Consider a start-up biotech, just emerging out the academic labs of Yale, UConn or Jackson Labs. The entrepreneur-founders face a daunting task: to bring a new medicine from laboratory concept to Food and Drug Administration-approved drug takes about 12 years and $2.7 *billion*. This means they must raise and raise again (and again) great sums from venture investors.

During that decade or more of innovative R&D, as the biotech is developing its new medicine, it will pay out that $2.7 billion as salary income to its employees, to contract research organizations, laboratory suppliers, law firms, accounting firms, and for clinical trials to test again and again safety and efficacy. To pay all those R&D bills, at any given time during that decade of drug development, the start-up biotech will have tens of millions of investor dollars in its corporate bank account.

Bear in mind that, at this stage, the biotech has no product, no income, only expenses. But Connecticut taxes the biotech on its bank account balance.

Since the biotech in my example has no income, it does not pay the 9% state income tax. But it does have a large bank account balance—a capital base—to pay all its bills.

If the biotech has an average balance of $20 million—which is typical, with many companies having balances several times as large—it would owe Connecticut $62,000. This is about the starting salary of a biotech scientist.

It is also a thorn in the side of entrepreneurs. Few other states have a capital base tax, none drain start-up coffers to the same extent as Connecticut.

Connecticut has made significant investments in the life sciences both to bring novel treatments and cures to patients *and* for economic development that the biopharma industry offers. Among many measures of its economic development value is the $55 billion the biopharma sector spends annually on research and development. This creates jobs with an average salary of $95,000 – 85% greater than the overall private sector average—and concomitant personal income tax revenue.

To attract biotech companies to Connecticut, to incentivize them to choose Connecticut over Boston-Cambridge, Roosevelt Island in New York, San Francisco or San Diego, we need to eliminate the capital base tax. It's unfair, levied not on income, but on money painstakingly raised and saved for R&D.

It is a shame that Connecticut policy would work to incentivize biotechs to set up operations or move elsewhere to avoid a tax that, while hugely consequential to them, is of de minimis value to the state. By removing the capital base tax we can help root cutting edge life sciences companies here and, in so doing, build a robust *income* tax base—corporate and personal—as our biotech companies' medicines reach pharmacy shelves.

I would be happy to answer any questions you may have or expand upon any points made in my testimony.

Thank you.