

Texas Adopts R&D Sales/Use Tax Exemption and Franchise Tax Credit Rules

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Overview

In 2013 Texas adopted into law House Bill 800 (“HB800”), which allowed taxpayers to elect to either claim a sales/use tax exemption for the purchase of tangible personal property used for research and development (“R&D”) activities or take an R&D credit against the franchise tax for qualifying research expenditures.¹ On March 27, 2015, the Texas Comptroller is scheduled to issue rules (effective April 5, 2015, and applicable to franchise tax reports originally due on or after January 1, 2014²) related to several of the new provisions, including rules concerning amended reports applicable where a taxpayer desires to claim a credit that was not claimed previously or to repay a credit taken previously and instead claim exemption from sales and use tax.³ In this Tax Alert we summarize the credit, the exemption and the new rules, focusing on the amended report procedures and requirements.

Sales/Use Tax Exemption

The sales/use tax exemption became effective January 1, 2014,⁴ and will expire on December 31, 2026.⁵ The exemption applies to the sale, storage or use of depreciable tangible personal property directly used in “qualified research” if the property is sold, leased, rented to or stored or used by a person who is engaged in “qualified research.”⁶ The exemption is not available if the taxpayer (or another member of the taxpayer’s combined franchise tax group) claims an R&D credit on its franchise tax return for the period.⁷

Taxpayers must register with the Comptroller’s office before claiming the exemption on qualifying purchases.⁸ Registration may be performed either by using the Comptroller’s online registration system or by filing Form AP-234, *Texas Registration for Qualified Research and Development Sales Tax Exemption*.⁹ Upon completion of the registration, the Comptroller will issue to the taxpayer a Texas Qualified Research Registration Number (“Registration Number”).¹⁰ Taxpayers must furnish a *Texas Qualified Research Sales and Use Tax Exemption Certificate* (Form 01-931) to the retailer when claiming the exemption and must file an Annual Information Report with the Comptroller’s office on or before March 31 of the year immediately following the calendar year in which they claimed the exemption.¹¹

Franchise Tax Credit

The R&D Credit is available on returns originally due on or after January 1, 2014, and will expire on December 31, 2026.¹² The amount of the credit is 5% of the difference between:

- the qualified research expenses incurred in Texas during the period on which the report is based; and

¹ Acts 2013, 83rd Leg., Reg. Sess., ch. 1266 (H.B. 800 adopted Jun. 14, 2013) §§ 2, 3, 6, 7. For more information regarding H.B. 800 and H.B. 500 (Acts 2013, 83rd Leg., Reg. Sess., ch. 1232 adopted Jun. 14, 2013), see our Tax Alert dated June 17, 2013, available [here](#).

² 34 Tex. Admin. Code § 3.599(a)(1).

³ 34 Tex. Admin. Code § 3.599, available [here](#). Note that the Comptroller’s website available [here](#) (last visited Mar. 23, 2015) provides: “A person cannot claim both the sales tax exemption and the franchise tax credit for the same period. The election to claim the sales tax exemption or take the franchise tax credit is not permanent and can be changed.”

⁴ Acts 2013, 83rd Leg., Reg. Sess., ch. 1266 (H.B. 800) §§ 5, 7.

⁵ Tex. Tax Code § 151.3182(f).

⁶ Tex. Tax Code § 151.3182(b). The term “qualified research” will have the same meaning as that applicable in I.R.C. § 41.

⁷ Tex. Tax Code § 151.3182(b)(2)).

⁸ See, Texas Comptroller of Public Accounts, Sales Tax Exemption or Franchise Tax Credit for Qualified Research Effective Jan. 1, 2014, available [here](#) (last visited Mar. 23, 2015).

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.*

¹² Acts 2013, 83rd Leg., Reg. Sess., ch. 1266 (H.B. 800) §§ 6, 7. Note, however, the expiration will not affect the unused credit carryforwards allowed under Tex. Tax Code §171.659. Tex. Tax Code § 171.665.

- 50% of the average amount of qualified research expenses incurred in Texas during the three tax periods immediately preceding the period on which the report is based.¹³

The tax credit is not available for any qualified research expense incurred in Texas during the period on which a report is based if the taxpayer (or another member of the taxpayer's combined franchise group) claims a sales/use tax exemption under Tex. Tax Code § 151.3182 during that period.¹⁴

If the taxable entity has no qualified research expenses in Texas in one or more of the three tax periods preceding the period on which the report is based, the credit for the period on which the report is based equals 2.5% of the qualified research expenses incurred in Texas during that period.¹⁵

The credit is limited to 50% of the amount of franchise tax due before any other applicable tax credits.¹⁶ The credit can be carried forward for 20 consecutive reports.¹⁷ Credits are considered to be used in the following order:

- R&D credit carryforward generated prior to January 1, 2008;
- R&D credit carryforward pursuant to H.B. 800; and
- Current year R&D credit.¹⁸

The R&D credit cannot be conveyed, assigned or transferred unless all the assets of the taxable entity are conveyed, assigned or transferred in the same transaction.¹⁹ A taxpayer must apply for the credit on the tax report for the period in which the credit is claimed.²⁰

New Comptroller Rules

The majority of the Comptroller's new rules mirror the statutory provisions discussed above as related to the franchise tax R&D credit.²¹ However, the rules include additional language providing a process for amending a franchise tax report, either to: (1) claim a credit that was not claimed previously; or (2) repay a credit taken previously for franchise tax purposes and instead claim exemption from sales and use tax for qualifying R&D purchases.²²

Under the new rules (effective April 5, 2015, and applicable to franchise tax reports originally due on or after January 1, 2014²³), the process for filing an amended report differs depending upon whether a taxpayer or a member of its combined reporting group had a Registration Number (issued by the Comptroller so that the taxpayer may claim the R&D sales tax exemption²⁴) for the period the taxpayer intends to claim a credit. If a taxpayer or a member of its combined reporting group did not have an active Registration Number for the period it intends to claim an R&D credit, the taxpayer or member of its combined group may file an amended report to claim the credit.²⁵

Alternatively, if a taxpayer or a member of its combined group had a Registration Number for the period it intends to claim an R&D credit, the taxpayer or member of the combined group must submit a written request to the Comptroller to cancel the registration before claiming the credit. Along with that request, the taxpayer must supply the following information: (1) the tax period for which it intends to claim the credit; (2) a statement whether sales and use tax exempt purchases were made and, if such purchases were made; (3) "an original or

¹³ Tex. Tax Code § 171.654(a). Note that if the taxable entity contracts with one or more public or private institutions of higher education for the performance of qualified research, the credit will be 6.25% of the difference referenced above. Tex. Tax Code § 171.654(b).

¹⁴ Tex. Tax Code § 171.653(a).

¹⁵ Tex. Tax Code § 171.654(c). Likewise, if the taxable entity contracts with one or more public or private institutions of higher education for the performance of qualified research, but has no qualified research expenses in Texas in one or more of the three tax periods preceding the period on which the report is based, the credit for the period on which the report is based equals 3.125% of all qualified research expenses incurred during that period. Tex. Tax Code § 171.654(d).

¹⁶ Tex. Tax Code § 171.658.

¹⁷ Tex. Tax Code § 171.659.

¹⁸ Tex. Tax Code § 171.659(1)-(3).

¹⁹ Tex. Tax Code § 171.660.

²⁰ Tex. Tax Code § 171.661.

²¹ 34 Tex. Admin. Code § 3.599.

²² 34 Tex. Admin. Code § 3.599(m).

²³ 34 Tex. Admin. Code § 3.599(a)(1).

²⁴ 34 Tex. Admin. Code § 3.599(b)(8).

²⁵ 34 Tex. Admin. Code § 3.599(m)(1). Note that this provision only applies if a report was originally due and filed after the effective date of 34 Tex. Admin. Code § 3.599 and a credit was not claimed. *Id.* As specified in 34 Tex. Admin. Code § 3.599(a)(1), 34 Tex. Admin. Code § 3.599 applies to "franchise tax reports originally due on or after January 1, 2014."

amended sales and use tax report with tax due, penalty and interest for the sales tax periods that cover the tax exempt purchases.”²⁶

In addition, if a report was filed claiming the R&D credit and a taxpayer later decides to instead claim a sales and use tax exemption, the taxpayer must: (1) file an amended franchise tax report that does not claim the credit and pay any tax, penalty and interest due; (2) apply for a Registration Number; and (3) file a request for a sales and use tax refund.²⁷

Contacts

If you have questions regarding the R&D exemption or credit, the Comptroller’s new rules or other Texas tax matters, please contact any of the following Deloitte Tax professionals.

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²⁶ 34 Tex. Admin. Code § 3.599(m)(2)(A), (B).

²⁷ 34 Tex. Admin. Code § 3.599(m)(3)(A)-(C).