



MULTISTATE TAX

Texas Comptroller proposes new treatment of research and development activities

Tax Alert

Overview

The Texas Comptroller of Public Accounts (“Comptroller”) recently published proposed regulatory amendments with the Office of the Texas Secretary of State to provide guidance on the franchise tax research and development (“R&D”) activities credit and the sales/use tax R&D exemption.¹ The publishing of the proposed amendments triggers a 30-day public comment period.² This tax alert summarizes the proposed amendments, effective dates, as well as offers some observations.

Modifications to Texas franchise tax R&D credit and Texas sales/use tax R&D exemption

The Comptroller has proposed to amend title 34 of the Texas Administrative Code (“TAC”) §§ 3.599 and 3.340 to provide clarity on the application of the franchise tax R&D credit and sales/use tax R&D exemption, respectively.

In relation to both the franchise tax R&D credit and the sales/use tax exemption, the proposed amendments add a definition for “business component” and expands the definition of “qualified research expense” to conform to the federal standard under Internal Revenue Code (“IRC”) § 41(b).³ Further, the proposed amendment incorporates the “Four-Part Test” under IRC § 174 and provides guidance on its application through hypothetical examples.⁴ The Comptroller’s proposed amendments also incorporate several minor revisions to improve readability.⁵

If the proposed amendment is ultimately adopted as a final regulation, the provisions will apply retroactively to Texas franchise tax reports due on or after January 1, 2014, along with Texas Qualified R&D Exemption Registrations made on or after January 1, 2014.⁶

Observations:

Taxpayers that have historically claimed the R&D activities credit for Texas franchise tax reporting purposes should continue to monitor the proposed regulations and ensure such activities qualify under 34 TAC § 3.599.

Taxpayers currently considering applying for or holding a Texas Qualified R&D Exemption Registration permit should consult with their tax advisors to help analyze any potential Texas sales/use tax implications.

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Footnotes

¹ Franchise Tax Margin: Research and Development Activities Credit, 46 Tex. Reg. 2565, 2565 (proposed April 6, 2021) (to be codified at 34 Tex. Admin. Code § 3.599) (Tex. Comptroller of Pub. Accounts); Limited Sales, Excise, and Use Tax: Qualified Research, 46 Tex. Reg. 2555, 2555 (proposed April 5, 2021) (to be codified at 34 Tex. Admin. Code § 3.340) (Tex. Comptroller of Pub. Accounts). A copy of the Texas Register issue is available [here](#).

² 46 Tex. Reg. at 2565, 2568.

³ Franchise Tax Margin: Research and Development Activities Credit, 46 Tex. Reg. 2568-69 (proposed April 6, 2021) (to be codified at 34 Tex. Admin. Code § 3.599) (Tex. Comptroller of Pub. Accounts); Limited Sales, Excise, and Use Tax: Qualified Research, 46 Tex. Reg. 2555, 2557 (proposed April 5, 2021) (to be codified at 34 Tex. Admin. Code § 3.340) (Tex. Comptroller of Pub. Accounts).

⁴ 46 Tex. Reg. at 2558, 2570.

⁵ 46 Tex. Reg. at 2555, 2565.

⁶ 46 Tex. Reg. at 2564, 2568.

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