

BILL ANALYSIS

Senate Research Center

H.B. 800
By: Murphy et al. (Deuell)
Finance
5/8/2013
Engrossed

AUTHOR'S / SPONSOR'S STATEMENT OF INTENT

According to interested parties, research and development activity creates high-paying jobs that provide substantial benefit to the Texas economy, new technologies and applications that generate economic efficiency and growth, and partnerships with institutions of higher education that expand opportunities for innovation and learning. These interested parties contend, however, that research and development in Texas has lagged behind other states in recent years to the point that Texas's share of the national expenditures for research and development is smaller than the state's share of the overall national economy, which these parties correlate to the removal of a tax credit for research and development. The parties cite a recent study that estimates that the lack of a research and development tax credit in Texas has cost the state more than \$3 billion annually and more than 20,000 jobs.

H.B. 800 seeks to make Texas economically competitive in the field of research and development by establishing a tax credit for research and development and consequently encouraging new investments, promoting the creation of high-paying jobs, and complementing Texas's manufacturing industries through innovation and efficiency.

H.B. 800 amends current law relating to a sales and use tax exemption and a franchise tax credit related to certain research and development activities.

RULEMAKING AUTHORITY

Rulemaking authority is expressly granted to the comptroller of public accounts of the State of Texas in SECTION 3 (Sections 171.654 and 171.662, Tax Code) of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1. LEGISLATIVE FINDINGS AND PURPOSES. (a) Provides that the legislature finds that:

- (1) Texas economic activity accounts for more than eight percent of the economic activity in the United States, but accounts for only five percent of research and development spending in the United States;
- (2) research and development activities create high-paying jobs that provide substantial benefits to the Texas economy, and new technologies and applications that generate economic efficiency and growth; and
- (3) private-sector research and development activities create partnerships between private-sector entities and institutions of higher education, and those partnerships expand opportunities for innovation and learning.

(b) Provides that the purposes of this Act, based on the findings specified in Subsection (a) of this section, are to:

- (1) make Texas economically competitive in the field of research and development;

- (2) reduce the tax burden on research and development activities in Texas and encourage new investments in this state;
- (3) promote the creation of new, highly skilled, high-paying jobs in Texas; and
- (4) complement this state's manufacturing industries by encouraging innovation and efficiency in applying new technologies and producing new products.

SECTION 2. SALES AND USE TAX EXEMPTION. Amends Subchapter H, Chapter 151, Tax Code, by adding Section 151.3182, as follows:

Sec. 151.3182. CERTAIN PROPERTY USED IN RESEARCH AND DEVELOPMENT ACTIVITIES; REPORTING OF ESTIMATES AND EVALUATION. (a) Defines, in this section, "depreciable tangible personal property," "Internal Revenue Code," and "qualified research."

(b) Provides that the sale, storage, or use of depreciable tangible personal property directly used in qualified research is exempted from the taxes imposed by this chapter if the property is sold, leased, or rented to, or stored or used by, a person who is engaged in qualified research, and will not, as a taxable entity as defined by Section 171.0002 (Definition of Taxable Entity) or as a member of a combined group that is a taxable entity, claim a credit under Subchapter M, Chapter 171, on a franchise tax report for the period during which the sale, storage, or use occurs.

(c) Requires the comptroller of public accounts of the State of Texas (comptroller) before the beginning of each regular session of the legislature, to submit to the legislature and the governor:

(1) an estimate of the total number of persons who received exemptions under this section and an estimate of the total amount of those exemptions; and

(2) an evaluation of the effect of the exemption under this section, in combination with the credit authorized by Subchapter M, Chapter 171, that is conducted by an independent researcher at a center for research authorized by Section 1.005 (Education Research Centers; Sharing Student Information), Education Code, on the amount of qualified research performed in this state, employment in research and development in this state, economic activity in this state, and state tax revenues.

(d) Requires the comptroller to require a person who receives an exemption under this section to complete a form to provide the information necessary for the comptroller to make the evaluation required by Subsection (c)(2). Provides that the information provided on the form is confidential and not subject to disclosure under Chapter 552 (Public Information), Government Code.

(e) Requires the comptroller to provide the estimates and evaluation required by Subsection (c) as part of the report required by Section 403.014 (Report On Effect of Certain Tax Provisions), Government Code.

(f) Provides that this section expires December 31, 2026.

SECTION 3. FRANCHISE TAX CREDIT. Amends Chapter 171, Tax Code, by adding Subchapter M, as follows:

SUBCHAPTER M. TAX CREDIT FOR CERTAIN RESEARCH AND DEVELOPMENT ACTIVITIES

Sec. 171.651. DEFINITIONS. Defines, in this subchapter, "Internal Revenue Code," "public or private institution of higher education," "qualified research," and "qualified research expense."

Sec. 171.652. ELIGIBILITY FOR CREDIT. Provides that a taxable entity is eligible for a credit against the tax imposed under this chapter in the amount and under the conditions and limitations provided by this subchapter.

Sec. 171.653. INELIGIBILITY FOR CREDIT FOR CERTAIN PERIODS. (a) Provides that a taxable entity is not eligible for a credit on a report against the tax imposed under this chapter for qualified research expenses incurred during the period on which the report is based if the taxable entity, or a member of the combined group if the taxable entity is a combined group, received an exemption under Section 151.3182 during that period.

(b) Provides that a taxable entity's ineligibility under this section for a credit on a report for the period on which the report is based does not affect the taxable entity's eligibility to claim a carryforward of unused credit under Section 171.659 on that report.

Sec. 171.654. AMOUNT OF CREDIT. (a) Provides that, except as provided by Subsections (b), (c), and (d), the credit for any report equals five percent of the difference between:

(1) the qualified research expenses incurred during the period on which the report is based, subject to Section 171.655; and

(2) 50 percent of the average amount of qualified research expenses incurred during the three tax periods preceding the period on which the report is based, subject to Section 171.655.

(b) Provides that the credit for the report, if the taxable entity contracts with one or more public or private institutions of higher education for the performance of qualified research and the taxable entity has qualified research expenses incurred in this state by the taxable entity under the contract during the period on which the report is based, equals 6.25 percent of the difference between:

(1) all qualified research expenses incurred during the period on which the report is based, subject to Section 171.655; and

(2) 50 percent of the average amount of all qualified research expenses incurred during the three tax periods preceding the period on which the report is based, subject to Section 171.655.

(c) Provides that, except as provided by Subsection (d), if the taxable entity has no qualified research expenses 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 percent of the qualified research expenses incurred during that period.

(d) Provides that the credit for the period on which the report is based equals 3.125 percent of all qualified research expenses incurred during that period if the taxable entity contracts with one or more public or private institutions of higher education for the performance of qualified research and the taxable entity has qualified research expenses incurred in this state by the taxable entity under the contract during the period on which the report is based, but has no qualified research expenses in one or more of the three tax periods preceding the period on which the report is based.

(e) Requires that, notwithstanding whether the time for claiming a credit under this subchapter has expired for any tax period used in determining the average amount of qualified research expenses under Subsection (a)(2) or (b)(2), the determination of which research expenses are qualified research expenses for purposes of computing that average be made in the same manner as that determination is made for purposes of Subsection (a)(1) or (b)(1). Provides that this subsection does not apply to a credit to which a taxable entity was entitled under Subchapter O (Tax Credit for Certain Research and Development Activities), as that subchapter existed before January 1, 2008.

(f) Authorizes the comptroller to adopt rules for determining which research expenses are qualified research expenses for purposes of Subsection (a) or (b) to prevent disparities in those determinations that may result from the taxable entity using different accounting methods for the period on which the report is based, as compared to any preceding tax periods used in determining the average amount of qualified research expenses under Subsection (a)(2) or (b)(2).

Sec. 171.655. **ATTRIBUTION OF EXPENSES FOLLOWING TRANSFER OF CONTROLLING INTEREST.** (a) Provides that, if a taxable entity acquires a controlling interest in another taxable entity or in a separate unit of another taxable entity during a tax period with respect to which the acquiring taxable entity claims a credit under this subchapter, the amount of the acquiring taxable entity's qualified research expenses equals the sum of:

(1) the amount of qualified research expenses incurred by the acquiring taxable entity during the period on which the report is based; and

(2) subject to Subsection (d), the amount of qualified research expenses incurred by the acquired taxable entity or unit during the portion of the period on which the report is based that precedes the date of the acquisition.

(b) Prohibits a taxable entity that sells or otherwise transfers to another taxable entity a controlling interest in another taxable entity or in a separate unit of a taxable entity during a period on which a report is based from claiming a credit under this subchapter for qualified research expenses incurred by the transferred taxable entity or unit during the period if the taxable entity is ineligible for the credit under Section 171.653 or if the acquiring taxable entity claims a credit under this subchapter for the corresponding period.

(c) Provides that the amount of the reimbursement, if during any of the three tax periods following the tax period in which a sale or other transfer described by Subsection (b) occurs, the taxable entity that sold or otherwise transferred the controlling interest reimburses the acquiring taxable entity for research activities conducted on behalf of the taxable entity that made the sale or other transfer, is:

(1) subject to Subsection (e), included as qualified research expenses incurred by the taxable entity that made the sale or other transfer for the tax period during which the reimbursement was paid; and

(2) excluded from the qualified research expenses incurred by the acquiring taxable entity for the tax period during which the reimbursement was paid.

(d) Prohibits an acquiring taxable entity from including on a report the amount of qualified research expenses otherwise authorized by Subsection (a)(2) to be included if the taxable entity that made the sale or other transfer described by Subsection (b) received an exemption under Section 151.3182 during the portion of the period on which the acquiring taxable entity's report is based that precedes the date of the acquisition.

(e) Prohibits a taxable entity that makes a sale or other transfer described by Subsection (b) from including on a report the amount of reimbursement otherwise authorized by Subsection (c)(1) to be included if the reimbursement is for research activities that occurred during a tax period under this chapter during which that taxable entity received an exemption under Section 151.3182.

Sec. 171.656. **COMBINED REPORTING.** (a) Requires that a credit under this subchapter for qualified research expenses incurred by a member of a combined group be claimed on the combined report required by Section 171.1014 (Combined Reporting; Affiliated Group Engaged In Unitary Business) for the group, and the combined group is the taxable entity for purposes of this subchapter.

(b) Authorizes an upper tier entity that includes the total revenue of a lower tier entity for purposes of computing its taxable margin as authorized by Section 171.1015 (Reporting for Certain Partnerships in Tiered Partnership Arrangement) to claim the credit under this subchapter for qualified research expenses incurred by the lower tier entity to the extent of the upper tier entity's ownership interest in the lower tier entity.

Sec. 171.657. **BURDEN OF ESTABLISHING CREDIT.** Provides that the burden of establishing entitlement to and the value of the credit is on the taxable entity.

Sec. 171.658. **LIMITATIONS.** Prohibits the total credit claimed under this subchapter for a report, including the amount of any carryforward credit under Section 171.659, from exceeding 50 percent of the amount of franchise tax due for the report before any other applicable tax credits.

Sec. 171.659. **CARRYFORWARD.** Authorizes a taxable entity, if the taxable entity is eligible for a credit that exceeds the limitation under Section 171.658, to carry the unused credit forward for not more than 20 consecutive reports. Provides that credits, including credit carryforwards, are considered to be used in the following order:

(1) a credit carryforward of unused credits accrued under Subchapter O before its repeal on January 1, 2008, and claimed as authorized by Section 18(d) (relating to authorizing a corporation that has any unused credits accrued to claim those unused credits on or with the tax report for the period in which the tax credit was accrued), Chapter 1 (H.B. 3), Acts of the 79th Legislature, 3rd Called Session, 2006;

(2) a credit carryforward under this subchapter; and

(3) a current year credit.

Sec. 171.660. **ASSIGNMENT PROHIBITED.** Prohibits a taxable entity from conveying, assigning, or transferring the credit allowed under this subchapter to another entity unless all of the assets of the taxable entity are conveyed, assigned, or transferred in the same transaction.

Sec. 171.661. **APPLICATION FOR CREDIT.** Requires a taxable entity to apply for a credit under this subchapter on or with the tax report for the period for which the credit is claimed.

Sec. 171.662. **RULES.** Requires the comptroller to adopt rules and forms necessary to implement this subchapter.

Sec. 171.663. **REPORTING OF ESTIMATES AND COLLECTION OF INFORMATION.** (a) Requires the comptroller, before the beginning of each regular session of the legislature, to submit to the legislature and the governor estimates of:

(1) the total number of taxable entities that applied credits under this subchapter against the tax imposed under this chapter, the total amount of those credits, and the total amount of unused credits carried forward.

(b) Authorizes the comptroller to require a taxable entity that claims a credit under this subchapter to complete a form to provide the information necessary for the comptroller to make the evaluations required by Section 151.3182. Provides that the information provided on the form is confidential and not subject to disclosure under Chapter 552, Government Code.

(c) Requires the comptroller to provide the estimates required by this section as part of the report required by Section 403.014, Government Code.

Sec. 171.664. DEPOSIT OF CERTAIN REVENUE. Requires the comptroller, notwithstanding any other law, for each fiscal year, to deposit to the credit of the property tax relief fund an amount of revenue received from the tax imposed under this chapter sufficient to offset any decrease in deposits to that fund that results from the implementation of this subchapter.

Sec. 171.665. EXPIRATION. (a) Provides that this subchapter expires December 31, 2026.

(b) Provides that the expiration of this subchapter does not affect the carryforward of a credit under Section 171.659 or a credit authorized under this subchapter established before the date this subchapter expires.

SECTION 4. INITIAL REPORTING OF INFORMATION. Requires the comptroller to submit the initial estimates required by Sections 151.3182(c)(1) and 171.663, Tax Code, as added by this Act, before the 84th Regular Legislative Session commences in January 2015. Provides that the comptroller, notwithstanding Section 151.3182(c)(2), Tax Code, as added by this Act, is not required to submit the initial evaluation required by that section until January 2017, but is required to submit that evaluation before the 85th Regular Legislative Session commences.

SECTION 5. TRANSITION PROVISION. Provides that Section 151.3182, Tax Code, as added by this Act, does not affect tax liability accruing before the effective date of this Act. Provides that tax liability accruing before the effective date of this act continues in effect as if this Act had not been enacted, and the former law is continued in effect for the collection of taxes due and for civil and criminal enforcement of the liability for those taxes.

SECTION 6. APPLICABILITY. Provides that Subchapter M, Chapter 171, Tax Code, as added by this Act, applies only to a report originally due on or after the effective date of this Act.

SECTION 7. EFFECTIVE DATE. Effective date: January 1, 2014.