

2009 Credit for Increased Research Activities - Individuals

Obtain additional information or assistance by calling one of the numbers listed below:

Phoenix	(602) 255-3381
From area codes 520 and 928, toll-free	(800) 352-4090
Hearing impaired TDD user	
Phoenix	(602) 542-4021
From area codes 520 and 928, toll-free	(800) 397-0256

Obtain tax rulings, tax procedures, tax forms and instructions, and other tax information by accessing the department's Internet home page at www.azdor.gov.

General Instructions

NOTE: THE 2009 FORM 308-I IS USED BY INDIVIDUAL TAXPAYERS. THE 2009 FORM 308 IS USED BY TAXPAYERS THAT ARE CORPORATIONS, S CORPORATIONS, OR PARTNERSHIPS.

ARS § 43-1074.01 provides a nonrefundable individual income tax credit for increased research activities in a taxable year. The credit for increased research activities applies to taxable years beginning January 1, 2001 and later.

The Arizona tax credit for individuals is allowed in an amount computed pursuant to IRC § 41 with the following exceptions:

- Qualified research includes only research conducted in Arizona. The term "qualified research," for purposes of the Arizona tax credit, means qualified research, as defined in IRC § 41, that is conducted in Arizona.
- The amount of the credit is based on the federal regular credit computation method for Arizona qualified research expenses. Taxpayers CANNOT use the federal alternative credit computation method. The allowable current taxable year credit is a percentage of the excess, if any, of the Arizona qualified research expenses for the taxable year over the base amount.

If the allowable expenses do not exceed \$2,500,000, the allowable credit is 20 percent of this amount. If the allowable expenses exceed \$2,500,000, the allowable credit amount is \$500,000 plus 11 percent of the amount of expenses over \$2,500,000, subject to certain limitations. The allowable credit limitation is the *lesser* of the amount computed above, or (a) \$1,500,000 (for taxable years beginning January 1, 2001 through December 31, 2001) or (b) \$2,500,000 (for taxable years beginning January 1, 2002 through December 31, 2002). For years beginning January 1, 2003 and later, the \$1,500,000 and \$2,500,000 limitations no longer apply.

- If two or more taxpayers, including shareholders of an S corporation and partners in a partnership, share in the eligible expenses, each taxpayer is eligible to receive a proportionate share of the credit.
- The termination provisions of IRC § 41 do not apply.

CARRYOVER OF UNUSED CREDIT

If the current taxable year credit for increased research activities exceeds your income tax liability for the current taxable year, you may carry forward the unused credit to the next 15

consecutive taxable years.

The amount of credit carryover that you may use to reduce your current year's tax liability is limited to the amount of tax liability that remains after you have used your current year's credit. If the carryovers are from taxable years beginning January 1, 2001 through December 31, 2002, the amount of credit carryover that may be used is further limited. This is addressed in the instructions for Part V of the Form 308-I.

If you have other nonrefundable tax credits that you are using to reduce your tax liability, you may not be able to use all of your credit for increased research activities to reduce your tax this year. You will be applying these limitations when you complete Form 301, *Nonrefundable Individual Tax Credits and Recapture*.

DO YOU HAVE TO MAKE OTHER ADJUSTMENTS TO ARIZONA GROSS INCOME OR TO THE ARIZONA TAX CREDIT FOR INCREASED RESEARCH ACTIVITIES?

- If you claim an Arizona credit for increased research activities for the taxable year, Arizona statutes do not require you to make an addition to Arizona gross income for the amount of qualified research expenses equal to the amount of the allowable Arizona credit.
- If you claim a reduced federal credit for increased research expenses and claim the Arizona credit for increased research activities, Arizona statutes do not require you to reduce the Arizona credit for increased research activities in a manner similar to the federal reduction method.
- If you reduce the amount of the deduction for qualified research activities in the computation of federal adjusted gross income, Arizona statutes do not allow you to take a subtraction from Arizona gross income for the amount of the expense reduction.
- If you adjust the federal asset basis of capitalized research expenses and reduce the amount of amortization deductible in the computation of federal adjusted gross income, Arizona statutes do not allow you to take a subtraction from Arizona gross income for additional amortization.

Specific Instructions

Complete the name and taxpayer identification number section at the top of the form. Indicate the period covered by the taxable year. Attach the completed form to the tax return.

All returns, statements, and other documents filed with the department require a taxpayer identification number (TIN). The TIN for an individual is the taxpayer's social security number or an IRS individual taxpayer identification number. Taxpayers that fail to include their TIN may be subject to a penalty.

Part I - Current Taxable Year's Credit Calculation (Sole Proprietorships Only)

NOTE: Complete this part only if you operate a business as a sole proprietorship and your sole proprietorship incurred qualified research expenses during the taxable year.

Line 1 -

Enter total wages paid or incurred for qualified services performed in Arizona. Do not include the amount of such wages

paid to employees that were used in the calculation of the federal work opportunity credit. Wages include any wages paid or incurred to an employee for qualified services performed by such employee. Qualified services consist of engaging in qualified research or engaging in the direct supervision or direct support of research activities that constitute qualified research.

Line 2 -

Enter the cost of supplies paid or incurred for use in the conduct of qualified research in Arizona. Supplies include expenditures for any tangible property other than land or improvements to land, and property of a character subject to the allowance for depreciation.

Line 3 -

Enter the amount paid or incurred to rent or lease the right to use computers in the conduct of qualified research in Arizona.

Line 4 -

Enter the total of:

- (a) Seventy-five percent (.75) of any amount paid or incurred for qualified research performed in Arizona by a qualified research consortium on your sole proprietorship's behalf. "Qualified research consortium" is any qualifying organization as defined in IRC § 41(b)(3)(C)(ii).
- (b) Sixty-five percent (.65) of any amount paid or incurred for qualified research performed in Arizona on your sole proprietorship's behalf, other than such amounts paid to a qualified research consortium. Prepaid contract research expenses are considered paid in the year the research is actually done.

Line 6 -

Enter the average annual Arizona gross receipts for the four taxable years preceding the taxable year for which the credit is being determined (the credit year). You may be required to annualize gross receipts for any short taxable year.

If 2009 is the first year the taxpayer is in business, the average annual Arizona gross receipts for the preceding taxable years is zero. If the taxpayer has been in business in Arizona for less than four taxable years prior to the credit year, then the average is the sum of annual Arizona gross receipts of the applicable period, divided by the number of taxable years.

Example: ABC Corporation began business in Arizona in 2007. Its annual Arizona gross receipts for 2007 were \$100,000. Its annual Arizona gross receipts for 2008 were \$200,000. Therefore, ABC Corporation's average annual Arizona gross receipts for the 2009 credit year is \$150,000 ([$\$100,000$ plus $\$200,000$] divided by 2).

Line 7 -

Round off the percentage to the nearest one, one hundredth of one percent (four decimal places). Compute the fixed-base percentage as follows:

- **Existing firms** - An existing firm is one that had both Arizona gross receipts and Arizona qualified research expenses for at least three taxable years beginning after

December 31, 1983, and before January 1, 1989. The fixed-base percentage is the ratio that the aggregate Arizona qualified research expenses for all taxable years beginning after 1983 and before 1989, bears to the aggregate Arizona gross receipts for such taxable years.

- **Start-up companies** - A start-up company is one that had both Arizona gross receipts and Arizona qualified research expenses either (1) for the first time in a taxable year beginning after December 31, 1983, or (2) for fewer than three taxable years beginning after 1983 and before 1989.

Fixed-Base Percentages for Taxable Years Beginning After 1993 in Which Start-Up Companies Incurred Arizona Qualified Research Expenses	
Taxable Year After 1993	Percentages for Taxable Years After 1993
1st through 5th	3 percent
6th	Divide the aggregate Arizona qualified research expenses for 4th and 5th taxable years by the aggregate Arizona gross receipts for 4th and 5th taxable years. Multiply the result by 1/6 (.1667).
7th	Divide the aggregate Arizona qualified research expenses for 5th and 6th taxable years by the aggregate Arizona gross receipts for 5th and 6th taxable years. Multiply the result by 1/3 (.3333).
8th	Divide the aggregate Arizona qualified research expenses for 5th through 7th taxable years by the aggregate Arizona gross receipts for 5th through 7th taxable years. Multiply the result by 1/2 (.50).
9th	Divide the aggregate Arizona qualified research expenses for 5th through 8th taxable years by the aggregate Arizona gross receipts for 5th through 8th taxable years. Multiply the result by 2/3 (.6667).
10th	Divide the aggregate Arizona qualified research expenses for 5th through 9th taxable years by the aggregate Arizona gross receipts for 5th through 9th taxable years. Multiply the result by 5/6 (.8333).
All years after 10th	Divide the aggregate Arizona qualified research expenses for any 5 taxable years selected by the taxpayer from among the 5th through 10th taxable years by the aggregate Arizona gross receipts for the selected taxable years.

If the percentage computation involves *de minimis* amounts of gross receipts and qualified expenses in a taxable year or short taxable years are involved, the amounts may be annualized or disregarded. Refer to IRC §§ 41(c)(3) and 41(f)(4) for details.

NOTE: The maximum percentage that can be entered on line 7 is 16 percent (.16).

Line 10 -

Multiply line 5 by 50 percent (.50). The base amount cannot be less than 50 percent of the current year qualified research expenses. This rule applies both to existing and start-up companies.

Line 12 -

Calculate the allowable credit amount according to the instructions in the following table. Enter the result.

Calculation of Current Taxable Year's Credit	
If the amount on line 11 is:	Credit Calculation
Equal to or less than \$2,500,000	Multiply the amount on line 11 by 20 percent (.20)
More than \$2,500,000	\$500,000 plus 11 percent (.11) of the amount on line 11 over \$2,500,000

Part II - Current Taxable Year's Credit Passed Through From S Corporations and Partnerships

Line 13 -

Enter the aggregate amount you received from S corporations and partnerships from Form 308, Part II, line 24, and Part III, line 27. Attach a copy of Form 308 received from S corporations or partnerships to your return.

As an S corporation shareholder or partner, you must complete Parts III and/or IV to compute the available carryover of the credit passed through by S corporations or partnerships. You should complete Parts III and/or IV only if your allowable credit for increased research activities for prior taxable years exceeded your Arizona income tax liability for those taxable years.

Part III - Available Pre-2003 Credit Carryover

Use Part III to compute the carryover of the credit for increased research activities from taxable years beginning January 1, 2001 through December 31, 2002. Since the credit for increased research activities applies only to individuals for taxable years beginning after December 31, 2000, there is no available credit carryover from taxable years beginning prior to January 1, 2001. Compute the total available carryover of the credit for increased research activities on page 1, Part III, lines 14 through 16.

In column (b), enter the credit originally computed for taxable year 2001 and 2002. In column (c), enter the amount of the credit from taxable years 2001 and 2002 which has already been used. Subtract the amount in column (c) from column (b) and enter the difference in column (d). Add the amounts entered on lines 14 and 15 in column (d). Enter the total on line 16, column (d). This is the total credit carryover available for years beginning before January 1, 2003.

Part IV - Available Post-2002 Credit Carryover

Use Part IV to compute the carryover of the credit for increased research activities from taxable years beginning on or after January 1, 2003.

In column (b), enter the credit originally computed for taxable years 2003 and subsequent years. In column (c), enter the amount that has already been used. Subtract the amount in column (c) from column (b) and enter the difference in column (d). Add the amounts entered on lines 17 through 22 in column (d). Enter the total on line 23, column (d). This is the total credit carryover available for years beginning on or after January 1, 2003.

Part V - Limitation of Credit Carryovers

Use Part V to figure the limitations on use of credit carryovers. Complete lines 24a through 27 if you claimed the credit on a prior year return and the credit was more than your tax.

LIMITATION FOR CREDIT CARRYOVERS FROM TAXABLE YEARS BEGINNING JANUARY 1, 2001 THROUGH DECEMBER 31, 2002. There is an additional limitation on how much you can use of your available credit carryovers included in the amount from Part III, line 16, column (d). To calculate the limitation, you must first compare the amount of your tax liability with \$500,000, and select the lower of those two numbers. Then, subtract your current year's credit for increased research activities from the number you selected. Use your entire current year's credit for increased research activities for this computation, even if you will not be able to claim that entire amount on your current year's tax return. If the result of your calculation is zero or less, you will not be able to use your credit carryforward from taxable years beginning January 1, 2001 through December 31, 2002, to reduce your current year's tax liability. However, you may still be able to use your credit carryover from 2003 and later.

LIMITATION FOR CREDIT CARRYOVERS FROM TAXABLE YEARS BEGINNING ON OR AFTER JANUARY 1, 2003. The amount of credit carryover from taxable years beginning on or after January 1, 2003, is only limited by the amount by which your current year's tax liability exceeds your current year's credit for increased research activities.

Line 24a -

Enter your tax liability from Form 301, Part II, line 32.

Line 24b -

Enter the current taxable year's credit from sole proprietorships from Part I, line 12.

Line 24c -

Enter the current taxable year's credit from pass through entities from Part II, line 13.

Line 24d -

Add lines 24b and 24c. Enter the result.

Line 24e -

Subtract line 24d from line 24a and enter the result.

Line 25a -

Enter your available pre-2003 credit carryover from Part III, line 16, column (d).

Line 25b -

If the amount on line 24a is lower than \$500,000, enter that number on line 25b. If it is not, enter \$500,000.

Line 25c -

Subtract line 24d from line 25b and enter the result. If the result is less than zero, enter zero.

Line 25d -

Compare the numbers on lines 25a and 25c, and enter the lowest number here. This is the amount of pre-2003 carryover you may use to reduce your current year's Arizona tax liability.

Line 26 -

Subtract line 25d from line 24e and enter the result.

Line 27 -

Compare the numbers on Part IV, line 23, column (d), and on Part V, line 26, and enter the lowest number here. This is the amount of post-2002 carryover you may use to reduce your current year's Arizona tax liability.

Part VI - Total Available Credit

Complete this section to compute the total available credit for the taxable year. The total available credit is the sum of the credit for current taxable year increased research activities and the available credit carryover(s).

Line 28 -

Enter the amount from Part V, line 24d. This is the current taxable year's credit for increased research activities.

Line 29 -

Enter the amount from Part V, lines 25d. This is the amount of the pre-2003 carryover that you may use to reduce your current year's Arizona tax liability.

Line 30 -

Enter the amount from Part V, line 27. This is the amount of the post-2002 carryover that you may use to reduce your current year's Arizona tax liability.

Line 31 -

Add the amounts on lines 28, 29, and 30. This is the total available credit for increased research activities that may be applied to your current taxable year's tax liability. Enter the total here and on Form 301, Part I, line 6.