

2013 Credit for Increased Research Activities - Individuals

CONTACTS FOR REFUND OF CREDIT FOR INCREASED RESEARCH ACTIVITIES

Arizona Commerce Authority

•Application forms •Program guidelines

Internet home page: www.azcommerce.com

Program Manager (602) 845-1200

CONTACTS FOR NONREFUNDABLE CREDIT FOR INCREASED RESEARCH ACTIVITIES

Arizona Department of Revenue

•Tax forms and instructions •Information and assistance

Internet home page: www.azdor.gov

Taxpayer assistance (602) 255-3381

From area codes 520 and 928, toll-free (800) 352-4090

General Instructions

NOTE: THE 2013 FORM 308-I IS USED BY INDIVIDUAL TAXPAYERS. THE 2013 FORM 308 IS USED BY TAXPAYERS THAT ARE CORPORATIONS, EXEMPT ORGANIZATIONS WITH UNRELATED BUSINESS TAXABLE INCOME, S CORPORATIONS, OR PARTNERSHIPS.

Arizona Revised Statutes (A.R.S.) § 43-1074.01 provides an individual income tax credit for increased research activities in a taxable year. For taxable years beginning from and after December 31, 2009, a portion of the current year's excess credit may be refundable to qualified taxpayers.

The credit for increased research activities is in lieu of the solar liquid fuel credit, provided by A.R.S. § 43-1085.01 (claimed on Arizona Form 344), with respect to the same expenses.

The Arizona tax credit for individuals is allowed in an amount computed pursuant to Internal Revenue Code (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.

For 2013, if the allowable expenses do not exceed \$2,500,000, the allowable credit is 24 percent of this amount. If the allowable expenses exceed \$2,500,000, the allowable credit amount is \$600,000 plus 15 percent of the amount of expenses over \$2,500,000.

- 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.

REFUND OF 75% OF CURRENT YEAR'S EXCESS CREDIT

If the current taxable year's credit for increased research activities exceeds your income tax liability for the taxable year, a portion of the excess credit may be refundable, if you qualify.

The amount of credit that is refundable is limited to 75% of the excess credit. The excess credit is the current year's credit less the current year's tax liability. The 75% refund is only available for the current year's excess credit for increased research activities. Once the taxpayer files a return with the department, the excess credit for increased research activities is carried forward; therefore, the taxpayer may not claim a refund for that taxable year.

NOTE: Because the refund is calculated after tax liability, it is necessary that you calculate all of your other credits before you can determine the current year's excess credit amount.

Taxpayers must apply to the Arizona Commerce Authority (Commerce) and receive a Certificate of Qualification (Certificate) to receive a refund. Taxpayers must have less than 150 full-time employees to qualify. The refund is the lesser of (a) 75% of the excess credit; or (b) the maximum refund on the Certificate from Commerce. Any additional amount is waived.

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 claim a proportionate share of the refund. An S corporation must apply for the Certificate on behalf of its shareholders. A partnership must apply for the Certificate on behalf of its partners.

Carryovers from the credit for increased research activities from previous taxable years will be carried over to the following taxable year, subject to the fifteen year carryover period and annual limitations on use of those carryovers.

CARRYOVER OF UNUSED CREDIT

If the current taxable year's 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 fifteen 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 VII of 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 Arizona 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 social security 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 Internal Revenue Service individual taxpayer identification number. Taxpayers that fail to include their TIN may be subject to a penalty.

Part I - Qualification for Refund of Current Taxable Year's Excess Credit**Line 1 -**

If your sole proprietorship applied to Commerce and received a Certificate related to the credit for increased research activities, check the "Yes" box. Otherwise, check the "No" box, and skip line 2.

Line 2 -

If you checked the "Yes" box on line 1, enter the maximum refund amount for taxable year 2013 on your Certificate from Commerce.

Line 3 -

If the entity from which you are claiming a pass through credit for increased research activities applied to Commerce and received a Certificate, check the "Yes" box. Otherwise, check the "No" box, and skip line 4 and line 5.

If you checked the "No" box for both line 1 and line 3, skip Part IV.

NOTE: *By checking the "No" boxes for both line 1 and line 3, you are indicating that you will not seek a refund for this taxable year, and instead will carry any excess credit forward. This election cannot be changed on an amended return.*

Line 4 -

If you checked the "Yes" box on line 3, enter the name and taxpayer identification number of the entity that received the Certificate from Commerce on line 4.

Line 5 -

If you checked the "Yes" box on line 3, enter your share of the maximum refund amount for taxable year 2013. Shareholders of an S corporation, enter the amount from Form 308, Part IV, line 34 or line 35. Partners of a partnership, enter the amount from Form 308, Part V, line 39 or line 40.

Part II - 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. If you received your credit as the result of a pass through, go to Part III.

Line 6 -

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 7 -

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 8 -

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

Line 9 -

Enter the total of:

- 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.

NOTE: *If your contract research expenses were made to an Arizona university under the jurisdiction of the Arizona Board of Regents and qualify as basic research payments, you may be entitled to an additional credit. See Arizona Form 346 for details.*

Line 11 -

Enter the amount of expenses included on lines 6 through 9 that are related to solar liquid fuel that will be claimed on Arizona Form 344. The credit for increased research activities is in lieu of the solar liquid fuel credit, provided by A.R.S. § 43-1085.01 (claimed on Arizona Form 344), with respect to the same expenses.

Line 13 -

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 2013 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 2011. Its annual Arizona gross receipts for 2011 were \$100,000. Its annual Arizona gross receipts for 2012 were \$200,000. Therefore, ABC Corporation's average annual Arizona gross receipts for the 2013 credit year is \$150,000 ([\$100,000 plus \$200,000] divided by 2).

Line 14 -

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 14 is 16 percent (.1600).*

Line 17 -

Multiply line 12 by 50% (.50). The base amount cannot be less than 50% of the current year qualified research expenses. This rule applies both to existing and start-up companies.

Lines 19 through 23 -

The way you compute the amount of the current year's credit you may receive depends on the amount of expenses you have. To determine your proper credit amount, complete lines 19 through 23 as instructed on the form.

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

Line 24 -

Enter the aggregate amount you received as a flow through from S corporations (from Form 308, Part IV, line 33) and partnerships (from Form 308, Part V, line 38). Attach a copy of Form 308 received from each S corporation or partnership to your return.

If you checked the "Yes" box on line 3, complete Part IV to calculate the amount of the current year's excess credit that is refundable to you.

Complete Part V and/or Part VI to compute the available carryover of the credit passed through by S corporations or partnerships from prior taxable years. You should complete Part V and/or Part VI only if your allowable credit for increased research activities for prior taxable years exceeded your Arizona income tax liability for those taxable years, and you did not receive a refund of the credit for increased research activities for those taxable years. The carry forward for tax years in which you received a refund of the credit for increased research activities is zero.

Part IV - Refundable Portion of the Current Taxable Year's Excess Credit

Only complete this section if you checked the "Yes" box in Part I, line 1 or Part I, line 3, and elect to receive a refund of 75% of your excess credit. The excess credit is the current taxable year's credit for increased research activities less the current taxable year's tax liability. Carryovers of the credit for increased research activities from previous taxable years will carry over for possible use in the next taxable year, provided they do not expire this taxable year.

NOTE: *If you complete Part IV and are receiving a refund, do not complete Part VII.*

Line 26 -

Enter the amount from Part III, line 25.

Line 27a -

Enter the amount from Form 140, line 23; or Form 140PY, line 26; or Form 140NR, line 26; or Form 140X, line 29.

Line 27b -

Enter the current year's nonrefundable tax credits from Form 301, excluding the credit or carryovers for increased research activities.

Line 27c -

Subtract line 27b from line 27a. Enter the difference. If the difference is zero or more, enter it on Part VIII, line 50; also enter it on Form 301, Part I, line 5, and Form 301, Part II, line 44. If the difference is less than zero, enter zero. This is the current year's credit for increased research activities that will be used to offset the current taxable year's tax liability.

Line 28 -

Subtract the amount on line 27c from line 26. Enter the difference. If the result is less than zero, enter zero, because no refund is available. This is the current year's excess credit.

Line 29 -

Multiply the amount on line 28 by 75% (.75) and enter the result. This is your tentative refundable credit.

Line 30 -

Enter the amount from Part I, line 2 or Part I, line 5. This is the maximum refundable credit.

Line 31 -

Enter the lesser of line 29 or line 30. Complete Part V and Part VI if you have carryovers from prior taxable years. Skip Part VII.

Enter the amount from line 31 on Form 140, line 33; or Form 140PY, line 35; or Form 140NR, line 33; or Form 140X, line 37. On the same line, be sure to check box 308-I indicating you are claiming a refundable credit for increased research activities.

NOTE: *If you complete Part IV and are receiving a refund, do not complete Part VII.*

Part V - Available Pre-2003 Credit Carryover

Use Part V 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 Part V, lines 32 through 34.

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 32 and 33 in column (d). Enter the total on line 34, column (d). This is the total credit carryover available for years beginning before January 1, 2003.

Part VI - Available Post-2002 Credit Carryover

Use Part VI 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 35 through 44 in column (d). Enter the total on line 45, column (d). This is the total credit carryover available for years beginning on or after January 1, 2003.

REMINDER: *If you received a refund of the credit for increased research activities in 2010, 2011, or 2012, no carryover is available in those years. In this case, enter zero in column (d) for those tax years.*

Part VII - Limitation of Credit Carryovers

Use Part VII to figure the limitations on use of credit carryovers. Complete lines 46a through 49 if you claimed the credit on a prior year return and the credit was more than your tax.

NOTE: *If you completed Part IV and are receiving a refund, do not complete Part VII.*

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 V, line 34, 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 46a -

Enter your tax liability from Form 301, Part II, line 37.

Line 46b -

Enter the current year's total credit from Part III, line 25.

Line 46c -

Subtract line 46b from line 46a and enter the difference. If the difference is zero or less, enter zero.

Line 47a -

Enter your available pre-2003 credit carryover from Part V, line 34, column (d).

Line 47b -

If the amount on line 46a is lower than \$500,000, enter that number on line 47b. If it is not, enter \$500,000.

Line 47c -

Subtract line 46b from line 47b and enter the difference. If the result is zero or less, enter zero.

Line 47d -

Compare the numbers on lines 47a and 47c, 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 48 -

Subtract line 47d from line 46c and enter the difference.

Line 49 -

Compare the amounts on Part VI, line 45, column (d), and on Part VII, line 48, and enter the lowest amount here. This is the amount of post-2002 carryover you may use to reduce your current year's Arizona tax liability.

Part VIII - Total Available Nonrefundable Credit

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

Line 50 -

If you completed Part IV and are receiving a refund, enter the amount from Part IV, line 27c. Otherwise, enter the amount from Part III, line 25. This is the current taxable year's credit for increased research activities.

Line 51 -

If you completed Part IV and are receiving a refund, enter zero. Otherwise, enter the amount from Part VII, line 47d. This is the amount of the pre-2003 carryover that you may use to reduce your current year's Arizona tax liability.

Line 52 -

If you completed Part IV and are receiving a refund, enter zero. Otherwise, enter the amount from Part VII, line 49. This is the amount of the post-2002 carryover that you may use to reduce your current year's Arizona tax liability.

Line 53 -

Add the amounts on lines 50, 51, and 52. 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 Arizona Form 301, Part I, line 5.