

Oregon Research & Development Tax Credit

Credit Mechanics and Other States

Joint Committee on Tax Expenditures

5/23/2023 | LRO



Overview of Presentation

- Topic: Federal and state level research and development tax credits
- Purpose of the credit
- Defining research & development
- Credit mechanics
- Policy parameters
- Other states





Purpose of the Tax Credit

- General purpose (federal)
 - Stimulate increased research and development (R&D) investment
 - Lower the cost to companies of undertaking R&D, thereby encouraging additional investment
 - Spillover effects, companies not capturing all returns of R&D
- Oregon
 - Policy of Oregon's expired tax credit
 - "encourage research in Oregon", and
 - "provide a good climate for business"
 - Leveraging federal incentives (CHIPS Act)
 - Competitiveness with other states



Defining Research & Development





What is Research & Development

- Oregon credit based on federal credit definitions
- **‘Qualified Research’ defined**
 - Experimental and aimed at the development of a new or improved product or process
 - Seek to gain new technical knowledge useful in development of new/improved business component (product, process, computer software technique, formula, invention, etc.)
 - Research includes process of experimentation
- **‘Basic Research’ defined**
 - Amount paid to qualified organization for basic research pursuant to written agreement (e.g. universities, federal laboratories, research consortia)



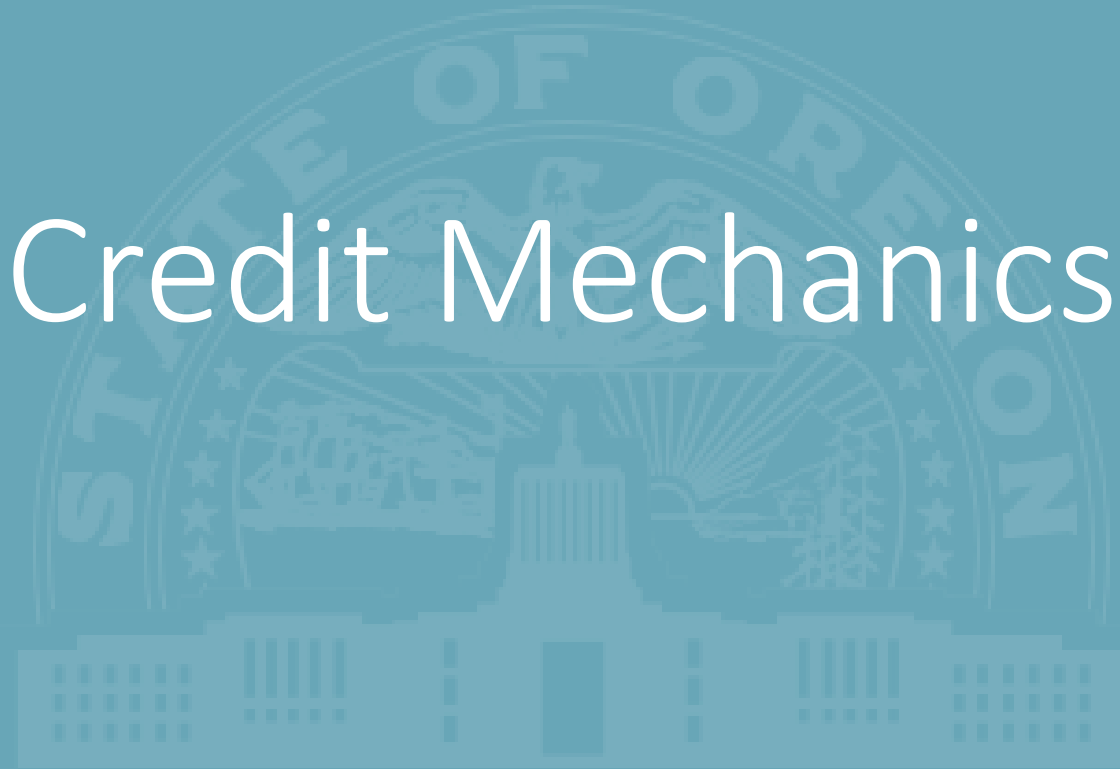


What is Research & Development

- Expenses eligible for the credit
 - Wages and salaries of employees/supervisors directly engaged in qualified research
 - Cost of materials and supplies used in such research
- Not eligible
 - Expenditures for equipment and structures
 - Fringe benefits
 - Overhead costs
- Approximate share of credit expenses (U.S.)
 - 70% wages/salaries
 - 15% materials/supplies
 - 15% contract research



Credit Mechanics





R&D Tax Credit

- Credit based on federal R&D tax credit
- Concept
 - Credit is a percentage of R&D expenditures above a historical amount
- Two ways in which to determine credit amount
 - Taxpayer claims the greater of the two calculations
 - 1) Regular credit
 - 2) Alternative simplified credit





R&D Tax Credit

- Credit based on federal R&D tax credit

QRE_t = Qualified Research Expenses in OR (in-house & contracted out)

$$\textit{Credit Amount} = \textit{Credit \%} * (QRE_t - \textit{base amount})$$





R&D Tax Credit

- Credit based on federal R&D tax credit

QRE_t = Qualified Research Expenses in OR (in-house & contracted out)

$$\textit{Credit Amount} = \boxed{\textit{Credit \%}} * (QRE_t - \textit{base amount})$$

Policy Lever
OR %





R&D Tax Credit

- Credit based on federal R&D tax credit

QRE_t = Qualified Research Expenses in OR (in-house & contracted out)

$$\textit{Credit Amount} = \boxed{\textit{Credit \%}} * (\textit{QRE}_t - \textit{base amount})$$





R&D Credit Calculations

$$\textit{Credit Amount} = \textit{Credit \%} * (\textit{QRE}_t - \textit{base amount})$$

- Concept
 - Base amount
 - Historical amount of R&D expenditures (floor of R&D expenditures)
 - Amount above base amount “excess amount”
- Difference between ‘regular credit’ and ‘alternative simplified credit’ is the base amount





Regular Credit: Base Amount

$$\textit{Credit Amount} = \textit{Credit \%} * (\textit{QRE}_t - \textit{base amount})$$

- Base amount:

$$\textit{Base amount} = \max\left[50\% * \textit{QRE}_t, \textit{FP} * \frac{\sum_{t-4}^{t-1} \textit{GR}}{4}\right]$$





Regular Credit: Base Amount

$$\textit{Credit Amount} = \textit{Credit \%} * (\textit{QRE}_t - \textit{base amount})$$

- Base amount:

$$\textit{Base amount} = \max\left[50\% * \textit{QRE}_t, \textit{FP} * \frac{\sum_{t-4}^{t-1} \textit{GR}}{4}\right]$$





Regular Credit: Base Amount

$$\textit{Credit Amount} = \textit{Credit \%} * (\textit{QRE}_t - \textit{base amount})$$

- Base amount:

$$\textit{Base amount} = \max\left[50\% * \textit{QRE}_t, \textit{FP} * \frac{\sum_{t-4}^{t-1} \textit{GR}}{4}\right]$$

Half of Qualified
Research Expenses
(QRE)





Regular Credit: Base Amount

- Base amount:

$$\text{Base amount} = \max\left[50\% * QRE_t, FP * \frac{\sum_{t-1}^{t-4} GR}{4}\right]$$

Concept

- Historical share of qualified research expenditures as percent of historic gross receipts
- FP= Fixed percentage
 - Fixed percentage is ratio of historic QREs to historic gross receipts, max 16%, fixed 3% for startups
- GR= Gross receipts





Regular Credit: Base Amount

- Base amount:

$$\text{Base amount} = \max\left[50\% * QRE_t, FP * \frac{\sum_{t-4}^{t-1} GR}{4}\right]$$

Average annual gross receipts during previous 4 years





Alternative Simplified Credit: Base Amount

$$\textit{Credit Amount} = \textit{Credit \%} * (\textit{QRE}_t - \textit{base amount})$$

Concept

- Base amount is half of previous three-year average of qualified research expenses

$$\textit{Base amount} = 50\% * \left(\frac{\sum_{t-3}^{t-1} \textit{QRE}_t}{3} \right)$$



Policy Parameters





R&D Credit: Oregon Policy Parameters

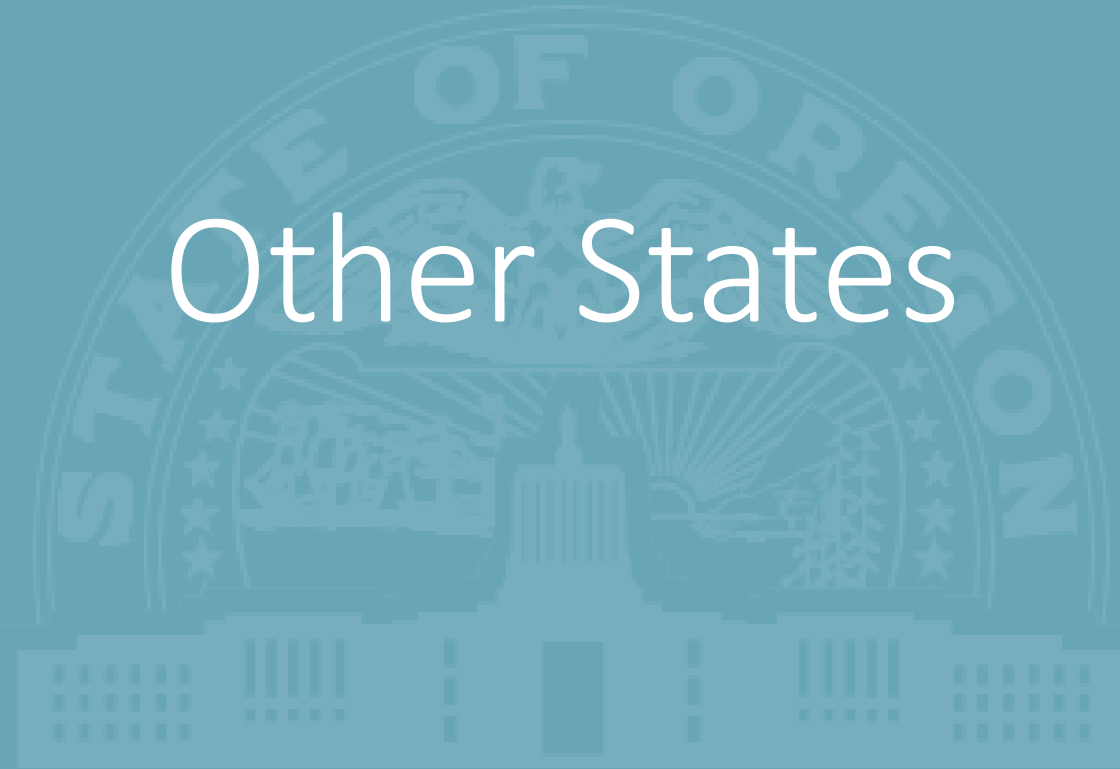
$$\textit{Credit Amount} = \textit{Credit \%} * (\textit{QRE}_t - \textit{base amount})$$

Policy proposals (SB 5 -5)

- Credit percentage: 25%
- Maximum credit amount per taxpayer
 - \$10M
 - \$5M, employs < 150 employees
- Credit refundability
 - Taxpayer < 2,000 employees anywhere
 - Taxpayer < 500 OR employees 100% refundable
 - Taxpayer: 500 - 2,000 OR employees, 50% refundable
- Type of business
 - 'Qualified semiconductor company'



Other States





Other States

- Majority of states have an R&D tax credit based on federal tax code
- Variance in tax credit percentage, limits, etc.
- Incentives do not exist in isolation





Other states

- Arizona
 - Tiered approach, credit rate: 24% to 15% (excess amount above \$2.5M)
 - \$100K capped refundability for taxpayers < 150 employees (\$5M cap in 2023)
- California
 - Credit rate: 15% of QRE, 24% of basic research
 - Additional (potentially expanded) credit calculation as compared to federal
- Florida
 - Credit rate: 10%, limited to 50% of tax liability
 - Limitation on sectors (sectors include: manufacturing, aviation & aerospace, IT, marine sciences)
- Idaho
 - Credit rate: 5%





Other states

- Ohio
 - Credit rate: 7%, applied against Ohio CAT
- Texas
 - Credit rate: 5%
 - Applied against franchise taxes or sales/use tax
 - Limited to 50% of tax due



Legislative Revenue Office

<https://www.oregonlegislature.gov/lro>

503-986-1266

State of Oregon

LEGISLATIVE REVENUE OFFICE

