Secure Oregon's Position as a Leader in Innovation

Renew the Research & Development Tax Credit

- Private investments in research and development (R&D) activities are the backbone of the modern economy. R&D activities account for nearly three percent of Oregon's gross state product.[1] These investments foster a business climate that contributes to the vibrant livability of our communities, the creation of thousands of jobs, billions in private investment dollars, downstream spending and support of the research industry.

- The modern economy is built on widgets and, in particular, the *next widget*. Businesses whose innovation becomes stagnant simply cannot survive. Sustained investments in R&D are the lifeblood of the modern business model and the bedrock of Oregon's economic future.

- The mobility of the research workforce allows such work to be performed virtually anywhere. Competition among states to attract these long-term, high-paying jobs and capital investments runs high because they generate valuable revenue for state and local governments. This is especially true for states highly dependent on personal income taxes to fund important public services and programs.

- Research facilities lost to another jurisdiction are very difficult to lure back due to the expenses associated with relocating operations.

- The R&D Tax Credit is intentionally designed to not be a corporate handout. A business cannot simply claim the credit for their existing research activities. Instead, a business must continually increase its investment in its workforce and equipment to qualify for the credit.

- Oregon's vision is to be a leader in research and innovation to enhance our economic prosperity. The research credit is a valuable economic tool anchoring businesses performing these activities today and providing an incentive to attract new employers in the future. Any erosion of this tool will simply discourage private investment in our state.

- As a matter of practice, Oregon businesses are continually analyzing and supporting their divisions that drive sustained growth and allow them to create jobs and innovative products. Oregon can do this too by renewing the R&D Tax Credit.

The Smart Growth Coalition urges you to VOTE YES on renewing the R&D Tax Credit.

[1] https://www.nsf.gov/statistics/2016/nsb20161/uploads/1/13/tt08-39.pdf

Mechanics of the R&D Tax Credit

The accounting requirements for the R&D Tax Credit can be complicated for non-accountants. Oregon connects to the definitions and requirements of the federal credit, outlined in IRC 41. As is typical for tax accounting, the formulas to determine the amount a taxpayer can claim for the credit are difficult to comprehend. Below is a simplified summary of the qualifications and formulas used to determine a taxpayer's eligibility for the credit.

Qualifying Expenses

IRC 41 allows for four types of expenses to qualify for the credit: wages, supplies, contract research, and basic research expenses (research that focuses on evaluating theories and hypotheses regardless of an application). Additionally, the revenue code strictly prohibits certain types of activities from being claimed for the credit to prevent abuse.

These prohibited activities include:

- Research conducted after the beginning of commercial production of the business component;
- Adaptation of existing business components;
- Duplication of existing business components;
- Reverse Engineering;
- Surveys, studies, activity relating to management function/technique, market research, routine data collection, or routine testing/quality control;
- Software developed for internal use;
- Foreign research conducted outside the United States, the Commonwealth of Puerto Rico, or any possession of the United States;
- Research related to social sciences, arts, or humanities;
- Research to the extent funded by any grant, contract, or otherwise by another person (or governmental entity).

Credit Calculation

There are two methods of calculating the credit. The most common method is the Standard Credit, which is a credit of 5 percent of qualifying expenses (listed above) compared to the taxpayer's historical investment (called the "base amount"). The base amount is determined by a fixed percentage in IRC §41(c)(3) multiplied by the average annual gross receipts from the four preceding tax years. The minimum base amount is 50 percent of qualifying expenses for the current tax year. The second method is the Alternative Simplified Credit, which is a credit of 14 percent of the qualifying expenses exceeding 50 percent of the taxpayer's average expenses for previous three years.

A taxpayer must continually increase its R&D investments in Oregon to benefit from the credit.