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BEFORE THE APPEALS DIVISION
DEPARTMENT OF REVENUE
STATE OF WASHINGTON

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| In the Matter of the Petition For |) | <u>D E T E R M I N A T I O N</u> |
| Refund/Correction of Assessment of |) | |
| |) | No. 13-0037 |
| ... |) | |
| |) | Registration No. . . . |
| |) | |
| |) | Docket No. . . . |
| |) | |

RULE 24003; RCW 82.04.4452: RESEARCH AND DEVELOPMENT CREDIT – CALCULATION – APPORTIONMENT OF INCOME. Compensation for conducting qualified R&D equals 100% of the amount Taxpayer received for conducting qualified R&D in Washington, regardless of whether some of the income from that activity is apportioned outside of Washington.

Headnotes are provided as a convenience for the reader and are not in any way a part of the decision or in any way to be used in construing or interpreting this Determination.

Lewis, A.L.J. – Taxpayer protests the Department’s denial of a refund request regarding . . . the calculation of the high technology research and development business and occupation (“B&O”) tax credit (the “R&D Credit”). The petition is granted in part and denied in part.¹

¹ Identifying details regarding the taxpayer and the assessment have been redacted pursuant to RCW 82.32.410.

ISSUES:

. . . Must the calculation of the R&D Credit, under the provisions of RCW 82.04.4452 and WAC 458-20-24003 (“Rule 24003”), take into consideration the apportionment of income and the failure to file surveys in some years?

FINDINGS OF FACT:

. . . Taxpayer claimed a refund for the R&D Credit for 2002 [through] 2007. The Audit Division disallowed the credit for 2002 and 2003 because those years were beyond the statute of limitations. The Audit Division also disallowed the credit for 2005 and 2007 because Taxpayer failed to file the required annual survey in those years. Taxpayer asserts it is entitled to the credit for the years that were disallowed.

The Audit Division granted the credit for 2004 and 2006 as part of the audit. The credit was based on amounts Taxpayer received for conducting qualified R&D. The Audit Division first applied an apportionment formula² to the amounts received when calculating the credit. Taxpayer also disputes the amount of the credit that was allowed, asserting that the credit should be based on the amount received for conducting qualified R&D rather than an apportioned amount.

For 2008 and 2009, Taxpayer filed annual surveys, but did not claim a credit because of disagreement with Audit on how it should be calculated.

ANALYSIS:

. . . RCW 82.04.4452 provides a B&O tax credit for qualified research and development spending:

(1) In computing the tax imposed under this chapter, a credit is allowed for each person whose research and development spending during the year in which the credit is claimed exceeds 0.92 percent of the person's taxable amount during the same calendar year.

Taxpayer engaged in qualified R&D activities within Washington and had sufficient R&D expenditures to qualify for the credit under the provisions of RCW 82.04.4452(1).

The Audit Division denied Taxpayer’s request for allowance of the R&D credit for 2002 and 2003 because the refund request was outside the non-claim period. The non-claim statute, RCW 82.32.060(1), states in pertinent part that:

no refund or credit shall be made for taxes . . . paid more than four

² Taxpayer’s income is subject to apportionment under the provisions of RCW 82.04.460 for B&O tax purposes. Audit determined that the amount received for conducting qualified R&D should likewise be apportioned prior to calculating the R&D credit.

years prior to the beginning of the calendar year in which the refund application is made or examination of records is completed.

There is no provision contained in RCW 82.32.060 or any other statute that permits the Department to waive the provisions of the non-claim-statute. Accordingly, we conclude that the R&D credit cannot be allowed for the 2002 and 2003 period.

Taxpayer also appealed the denial of the R&D credit for 2005 and 2007. Laws of 2005, Ch 514, § 1003 amended RCW 82.04.4452 to provide:

(6)(e) If a person fails to file a complete annual survey required under this subsection with the department by the due date or any extension under section 1001 of this act, the person entitled to the credit provided in subsection of this section is not eligible to claim or assign the credit provided in subsection (2) of this section in the year the person failed to timely file a complete survey.

Here, Taxpayer did not file annual surveys in 2005 and 2007. RCW 82.04.4452 is clear that a taxpayer is not eligible to claim the R&D credit in those years.

With regard to 2004, 2006, 2008, and 2009, RCW 82.04.4452(2) allows calculation of the credit using either an expenditure or compensation method. A taxpayer may take the greater of the credit calculated by both methods

RCW 82.04.4452(2) provides:

(2) The credit shall be calculated as follows: (a) Determine the greater of the amount of qualified research and development expenditures of a person or eighty percent of amounts received by a person other than a public educational or research institution in compensation for the conduct of qualified research and development; (b) subtract 0.92 percent of the person's taxable amount from the amount determined under (a) of this subsection; (c) multiply the amount determined under (b) of this subsection by the rate provided in RCW 82.04.260(3) in the case of a nonprofit corporation or nonprofit association engaging within this state in research and development, and the person's average tax rate for every other person.

RCW 82.04.4452(2) and Rule 24003(19)(a) provide that the B&O tax credit for R&D activities is calculated by determining 80% of amounts received by the taxpayer in compensation for conducting qualified R&D and then subtracting 0.92 percent of the person's taxable income from those amounts received, etc.

The issue is whether, when calculating the R&D Credit based on 80% of the amounts received by the Taxpayer as compensation for conducting qualified R&D, the "amount received" is subject to apportionment. "Qualified research and development," as defined in RCW 82.04.4452(7)(c), [means] research and development activities "performed within this state." RCW 82.63.010(16), (18). [The general purpose of apportionment is to fairly determine the

amount of property or income that is attributable to a particular taxing jurisdiction. Because the “amounts received” are limited to qualified research and development activities performed in Washington, there is no reason to “apportion” these amounts.] Whether 100% of the amounts received from performing the [qualified] R&D in Washington was subject to Washington’s B&O tax is irrelevant in calculating the initial 80% amount in RCW 82.04.4452(2)(a). Only the next step of the calculation in RCW 82.04.4452(2)(b), which subtracts .92% of the person’s “taxable amount,” takes into consideration what proportion of the Taxpayer’s income is subject to Washington’s B&O tax. RCW 82.04.4452(7)(e). . . . We conclude that [“amounts received” in] compensation for conducting qualified R&D equals . . . the amount Taxpayer received for conducting qualified R&D in this state, regardless of whether some of the income from that activity is apportioned outside of the state. We remand this matter to the Audit Division for adjustment of the R&D Credit for 2004 and 2006, and calculation of the R&D Credit for 2008 and 2009.

DECISION AND DISPOSITION:

The appeal is granted in part and denied in part.

Dated this 13th day of February 2013