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# **2013 Income Tax Credit Review**

**Joint Legislative Income Tax  
Credit Review Committee**

**December 10, 2013**

**JLBC**

# Joint Legislative Income Tax Credit Review Committee

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- Annually reviews credits as determined in statute
- This year's review includes:
  - Research and Development (R&D) Credit
  - Pollution Control Equipment Credit
  - Taxes Paid for Coal Consumed in Generating Electrical Power Credit
- These credits were reviewed by the committee in 2003 and 2008

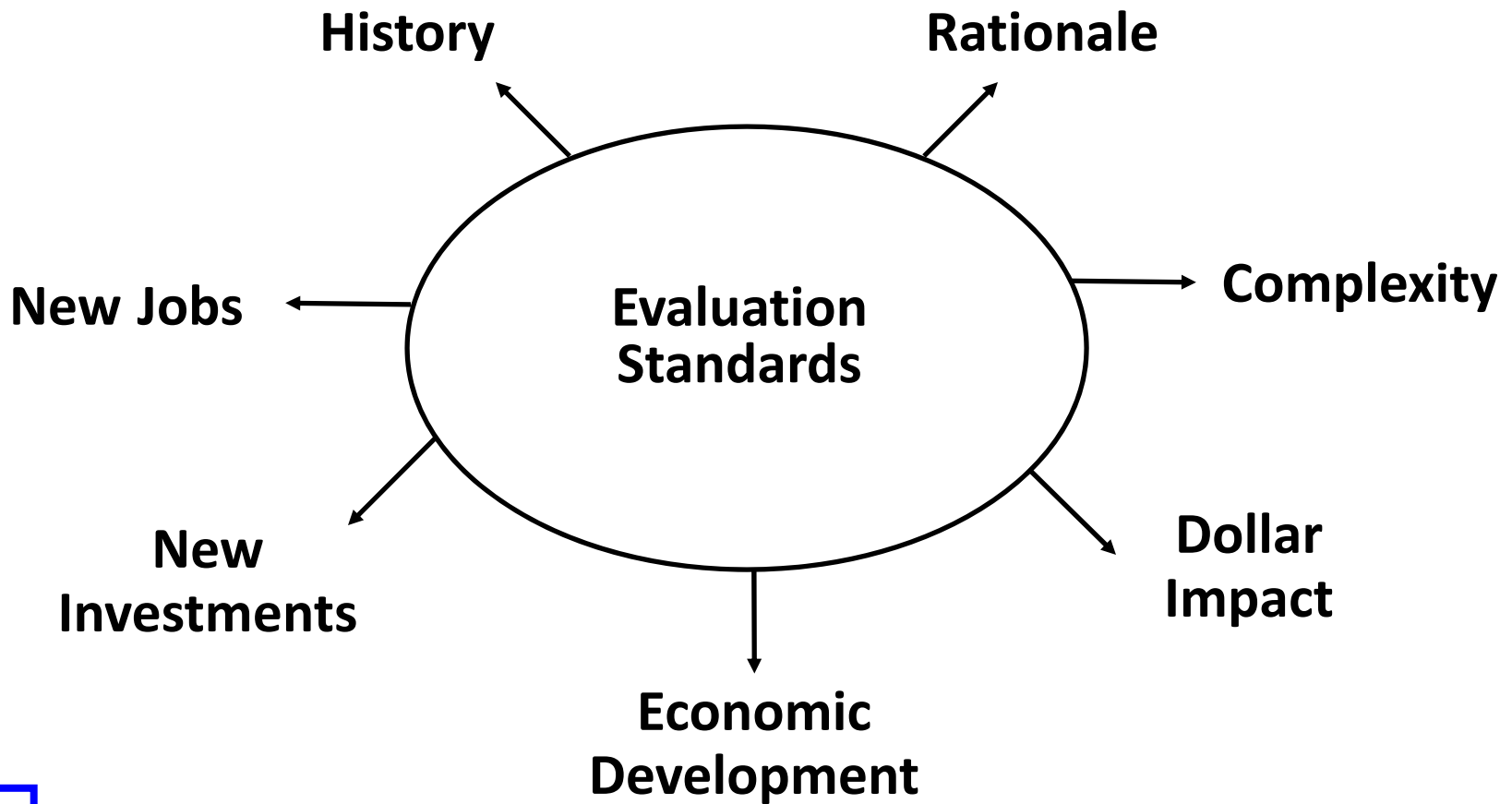
# Role of the Committee

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- Determine original purpose of tax credit
- Establish standards for evaluating and measuring success or failure
- Recommend changes

# Statute Provides Possible Standards

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# Confidential Taxpayer Information

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- ❑ Laws 2010, Chapter 225 authorizes DOR to disclose confidential “statistical information” only to the Committee and JLBC Staff
- ❑ DOR considers credit information confidential if:
  - credits were claimed by 3 or fewer taxpayers, or
  - a single taxpayer used more than 90% of total credits
- ❑ Two of the credits on the 2013 review schedule include confidential statistical information

# Issues Affecting Evaluation

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- Timeliness of data
- Lack of performance measures
- Certain costs and benefits can be difficult to quantify

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# Research and Development Tax Credit

# Research and Development Tax Credit

## - Summary

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- Cost – \$87 million in *nonrefundable* credits in 2011  
\$5 million in *refundable* credits approved
- Purpose – attract high-tech industry and remain competitive with other states
- Complexity – unusually complex in calculation and administration; record-keeping requirement can be burdensome
- Performance Measures – none in statute



# Research and Development Tax Credit

## – Description of the Credit

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- Credit is calculated based on same definitions as under federal R&D program
- Credit applies to R&D expenses above a certain base amount (“excess expenses”)
- If excess expenses  $\leq$  \$2.5m, credit is 24% of the amount; if excess expenses  $>$  \$2.5m, credit is \$600,000 plus 15% of the amount above \$2.5m

# Research and Development Tax Credit

## – Nonrefundable R&D Credit Program

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- Nonrefundable program consists of both the standard credit and an additional credit for university research
- University research credit is an additional 10% over and above amount allowed under standard credit
- Standard research credit has no cap and allows unused amounts to be carried forward up to 15 years
- University research credit is capped at \$10 million annually and provides a 5-year carry forward

# Research and Development Tax Credit

## – Refundable R&D Credit Program

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- Credit is refundable for businesses with fewer than 150 full-time employees
- Refund is limited to 75% of the amount by which the credit exceeds the taxpayer's liability
- Remaining 25% of the excess credit must be forfeited
- Up to \$5 million in refundable credits can be authorized each year

# Research and Development Tax Credit

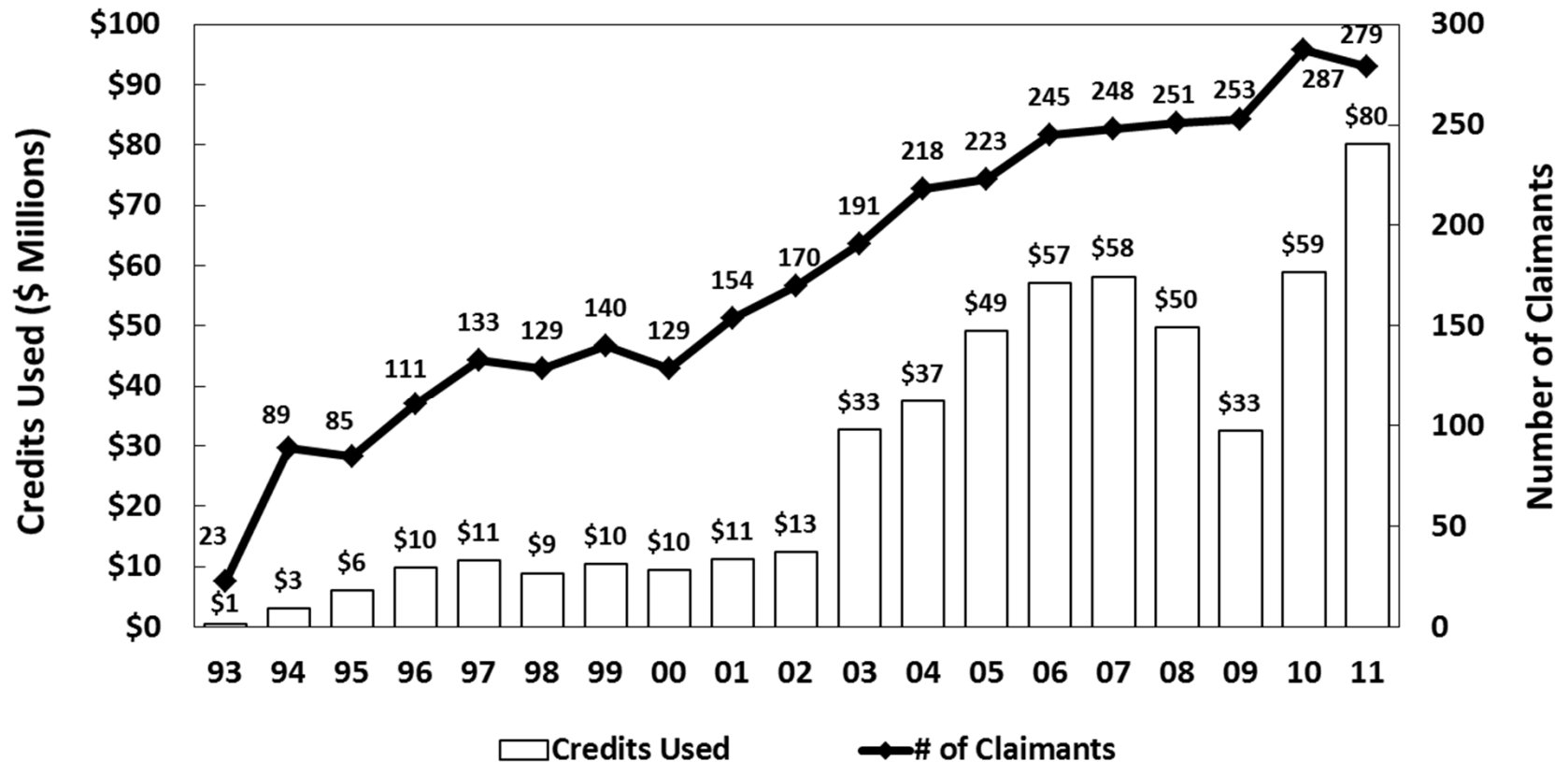
## – Carry Forward of Unused Credits

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- Credit carry forwards before 2003 are limited to \$500,000
- Credit carry forwards from and after 2003 are not limited
- However, unlimited carry forwards cannot exceed taxpayer's liability

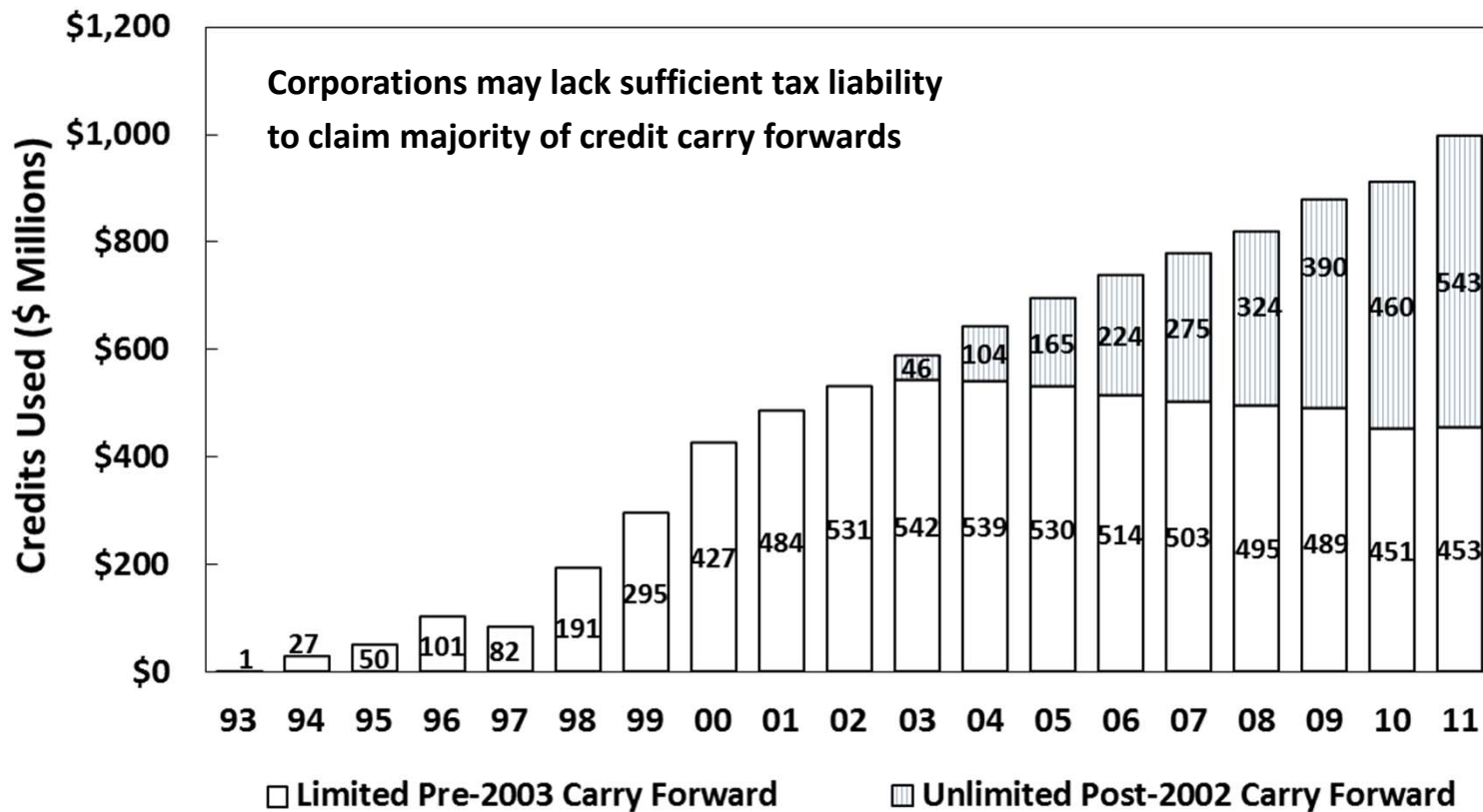
# Research and Development Credit (Corporate)

– Amount of Credits Used & Number of Claimants



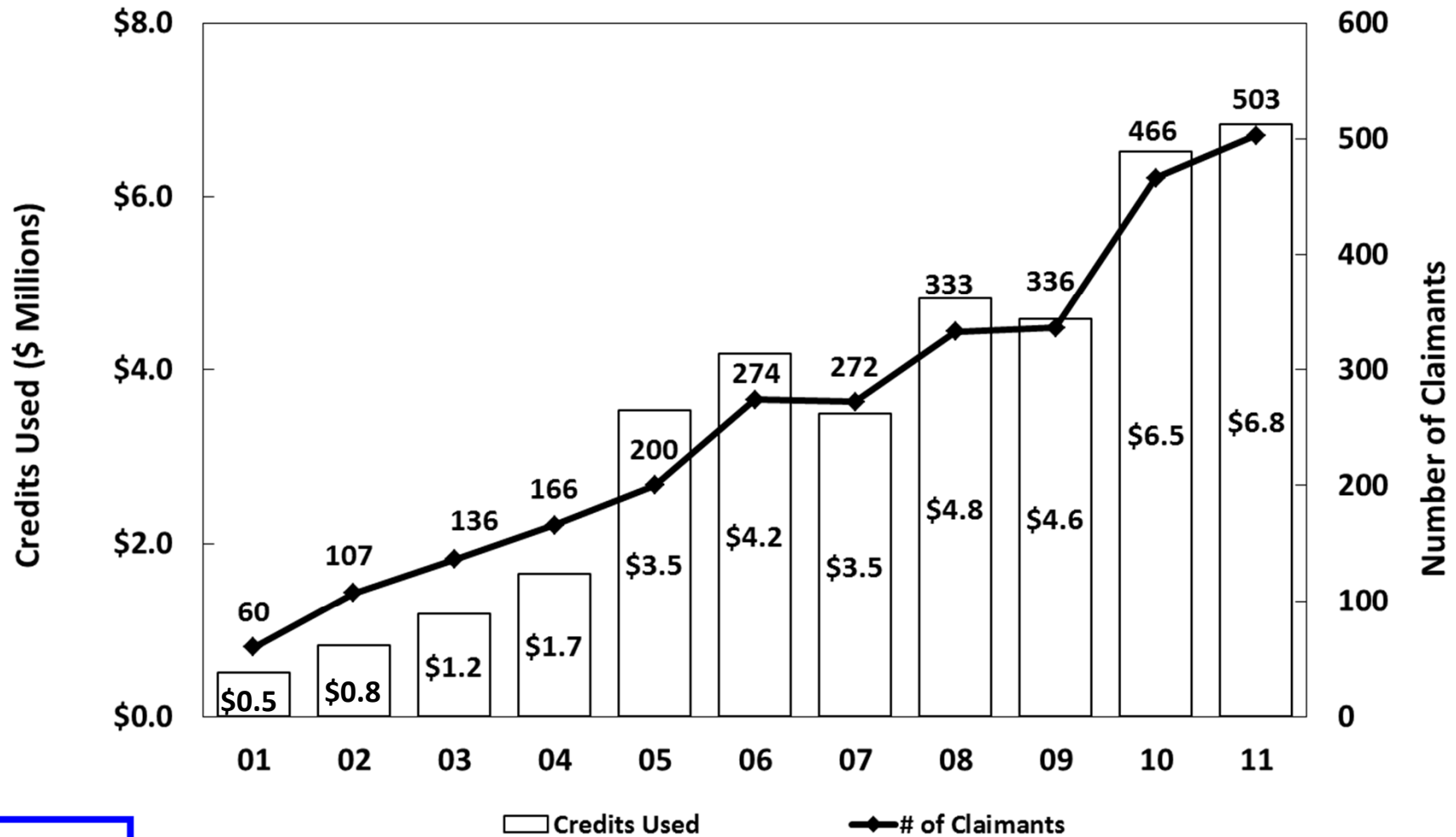
# Research and Development Credit (Corporate)

## – Amount of Limited and Unlimited Credit Carry Forward



# Research and Development Credit (Individual)

– Amount of Credits Used & Number of Claimants



# Research and Development Tax Credit

## – Benefits to the Arizona Economy

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- ❑ Qualified R&D spending since inception of program is about \$12 billion
- ❑ It is not known, however, how much of the R&D spending was directly attributable to the credit program
- ❑ Academic studies show varied results regarding the effectiveness of state R&D credits
- ❑ Impact of R&D program on Arizona jobs and investments is uncertain



# Research and Development Tax Credit

## – Potential Performance Measures

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- Total research dollars spent in Arizona each year
- Numbers of persons employed in research activities
- Total research payrolls
- Introduction of new products as a result of R&D activities
- Last reviewed in 2008
  - Committee recommended the continuation of the credit with enhanced performance measures.