

Instructions for 2004 Schedule R

General Instructions

Purpose of Schedule R

A corporation other than a tax-option (S) corporation uses Schedule R to compute and claim the credits for (1) increasing research activities in Wisconsin and (2) constructing and equipping new facilities or expanding existing facilities used for qualified research in Wisconsin. The corporation must attach Schedule R to its Wisconsin franchise or income tax return.

Who Is Not Eligible

Partnerships, limited liability companies (LLCs) treated as partnerships, tax-option (S) corporations, and individuals, including individual partners, members, and shareholders, cannot claim research credits.

Internal Revenue Code

For purposes of computing the Wisconsin research credits, "Internal Revenue Code" means the federal Internal Revenue Code (IRC) as amended to December 31, 2002, with certain exceptions that are explained in the Form 4 or Form 5 instructions. However, IRC section 41(h), relating to the termination of the federal credit, doesn't apply for Wisconsin purposes.

What Are Qualified Research Expenses

"Qualified research expenses" are defined in Internal Revenue Code section 41. They are the sum of in-house research expenses and 65% of contract research expenses (75% for payments made to qualified research consortia). See IRC section 41 for further details.

What Is Qualified Research

"Qualified research" is defined in IRC section 41. It means research for which expenditures may be treated as expenses under IRC section 174. This research must be undertaken for discovering information that is technological in nature, and its application must be intended for use in developing a new or improved business component of the taxpayer. In addition, substantially all of the activities of the research must be elements of a process of experimentation relating to a new or improved function, performance, reliability, or quality. See IRC sections 41 and 174 for a complete definition and special rules.

What Are Qualified Research Facility Expenditures

"Qualified research facility expenditures" are amounts paid or incurred during the taxable year to construct and equip new facilities or to expand existing facilities used in Wisconsin for qualified research. Eligible amounts include amounts paid or incurred for tangible, depreciable property, but do not include amounts paid or incurred for replacement property. See the tax release in *Wisconsin Tax Bulletin* 68, page 30, for more information.

Credits Are Income

The amount of credits constitutes income to the claimant and must be reported as income on the Wisconsin franchise or income tax return for the taxable year for which the credit is computed. Include the amount of credit computed on Schedule R on Form 4 or 5, Schedule V, line 9.

Carryover of Unused Credits

The research credits are nonrefundable. Any unused credit may be carried forward for 15 years. If there is a reorganization of a corporation claiming a research credit, the limitations provided by IRC section 383 may apply to the carryover of any unused Wisconsin research credit.

Adjustments for Certain Acquisitions and Dispositions

If a major portion of a trade or business is acquired or disposed of, adjustments must be made to qualified research expenses and gross receipts for the period before or after the acquisition or disposition. See IRC section 41(f)(3) for details.

Short Taxable Year

For any short taxable year, qualified research expenses or expenditures and gross receipts must be annualized.

Information

For more information, you may:

- E-mail your question to corp@dor.state.wi.us
- Send a FAX to (608) 267-0834
- Call (608) 266-2772 [TTY (608) 267-1049]
- Write to the Audit Bureau, Wisconsin Department of Revenue, Mail Stop 5-144, P.O. Box 8906, Madison, WI 53708-8906

Specific Instructions

Part I – Credit for Increasing Research Expenses

Line 1. Enter wages you pay to employees for actually doing research work, or for directly supervising or directly supporting research work, in Wisconsin. Generally, "wages" means the amount reported on the employee's wage statement, Form W-2. Include qualified wages that were used in computing the federal work opportunity tax credit.

Line 2. Enter the cost of supplies used in the conduct of qualified research in Wisconsin. "Supplies" are tangible property other than land, improvements to land, or depreciable property whether or not you take a depreciation deduction for it.

Line 3. Enter the amount paid for the rental or lease of computers used in qualified research in Wisconsin. Reduce this amount by the amount that you received for the right to use substantially identical property.

Line 4. Enter 65% of amounts paid under a contract for qualified research performed in Wisconsin by someone other than your employee. Prepaid contract research expenses are considered paid in the year the research is actually done.

Use 75% for payments made to a qualified research consortium in Wisconsin. A qualified research consortium is a tax-exempt organization described in IRC section 501(c)(3) or (6) that is organized and operated primarily to conduct scientific research and is not a private foundation.

Line 5. Enter any expenses used in computing the federal orphan drug credit that are Wisconsin qualified research expenses.

Note for Lines 1 through 5: Expenses incurred entirely outside Wisconsin may not be allocated to Wisconsin even if incurred for the benefit of research in Wisconsin. If qualified research expenses are incurred in and outside Wisconsin and the amount incurred in Wisconsin cannot be accurately determined, a portion of the qualified expenses may be reasonably allocated to Wisconsin.

Line 7. Enter the amount of any wages included on line 6 that qualify for the Wisconsin development zones credit. These wages may not be used in determining the Wisconsin research credit.

Section A – Regular Credit

Complete this section **only** if you are claiming the regular credit. You **cannot** change your election by filing an amended return.

Line 9. Complete lines 1 through 5 of the worksheet on back of Schedule R and enter the average annual Wisconsin gross receipts from line 5 on Schedule R, line 9.

On line 1 of the worksheet, enter the gross receipts for the 4 taxable years preceding the current taxable year (2000, 2001, 2002, and 2003). Reduce gross receipts for any taxable year by returns and allowances.

On line 2 of the worksheet, enter the portion of the total gross receipts included on line 1 that are not attributable to Wisconsin.

For purposes of the research credit, sales of tangible personal property are allocated to Wisconsin if (1) the property is delivered or shipped to a purchaser, other than the federal government, within Wisconsin, or (2) the property is

shipped from an office, store, warehouse, factory, or other place of storage in Wisconsin and delivered to the federal government within Wisconsin. "Throwback" sales are not treated as sales allocated to Wisconsin. Sales other than sales of tangible personal property are allocated to Wisconsin if the income-producing activity is performed in Wisconsin.

Line 10. Compute the Wisconsin fixed-base percentage as follows:

Existing companies (any company that isn't a start-up company) must complete lines 6 through 19 of the worksheet on back of Schedule R and enter the Wisconsin fixed-base percentage from line 19 on Schedule R, line 10. The Wisconsin fixed-base percentage is the ratio of the total qualified research expenses incurred in Wisconsin for at least 3 taxable years from 1984 to 1988 to the total gross receipts for those taxable years. **Note:** The maximum percentage that may be entered on line 10 is 16%.

Start-up companies having **both** gross receipts and qualified research expenses either (1) for the first time in a taxable year beginning after 1983, or (2) for fewer than 3 taxable years beginning after December 31, 1983, and before January 1, 1989, must enter 3% on line 10. **Note:** The fixed-base percentage for start-up companies is modified beginning with their 6th taxable year beginning after December 31, 1993. See IRC section 41 for details.

Section B – Alternative Incremental Credit

Complete this section **only** if you are electing the alternative incremental credit instead of the regular credit. The election is made by filling in Section B. You may make different elections for federal and Wisconsin purposes. Once made, the election applies to the current taxable year and all later taxable years, unless you receive the Department of Revenue's consent to revoke the election. You **cannot** change your election on an amended return. For more information, see the tax release in *Wisconsin Tax Bulletin 137*, page 31.

Line 16. See the instructions for Schedule R, line 9.

Part II – Credit for Research Facilities

Line 31. Enter the qualified research facility expenditures, as defined earlier. The expenditures in Part II do not include any expenses that are includable as qualified research expenses in Part I.