Instructions for 2015 Schedule R

General Instructions

Purpose of Schedule R

Individuals, estates and trusts, partnerships, corporations, tax-option (s) corporations, and exempt entities use Schedule R to compute and claim the credits for increasing research activities in Wisconsin.

See "**Special Instructions for Combined Group Members**," page (2) of these instructions for special rules that apply to combined group members of a corporation.

For more details on the research credit, see Publication 131 – *Tax Incentives for Conducting Qualified Research in Wisconsin*, available at: https://www.revenue.wi.gov/html/taxpubs.html

Only include one type of research credit on Schedule R. If you are eligible for more than one research credit, use additional Schedules R. For example, if you qualify for the credit for increasing research expenses and the credit for activities related to internal combustion engines, complete a separate Schedule R to compute the credit for increasing research expenses and another Schedule R to compute the credit related to internal combustion engines.

- Use one **Schedule R** for qualified research related to designing internal combustion engines and vehicles, including vehicles that are powered by such engines and improving production processes for such engines and vehicles.
- Use one **Schedule R** for qualified research related to the design and manufacturing of energy efficient lighting systems, building automation and control systems, or automotive batteries for use in hybrid-electric vehicles that reduce the demand for natural gas or electricity or improve the efficiency of its use.
- Use one **Schedule R** for all other types of qualified research.

The claimant must attach Schedule(s) R to its Wisconsin income or franchise tax return.

Who Is Not Eligible

Partnerships, limited liability companies (LLCs) treated as partnerships, and tax-option (S) corporations cannot claim research credits; however, the computation of, and eligibility for, the research credits are based on the research activities conducted by those entities. The credits computed at the entity level flow through to the partners, members, or shareholders based on their ownership interests and are claimed on their respective tax returns.

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, 2013, with certain exceptions that are explained in the Form 1, 1NPR, 2, 3, 4, 4T, 5S, or 6 instructions.

Relating to the Wisconsin research credits, exceptions to the IRC include:

- Section 41(f)(1), which provides special rules for the aggregation of expenditures for a controlled group of taxpayers filing a federal consolidated return
- Section 41(f)(2), which provides for special allocations in the case of estates, trusts, and partnerships
- Section 41(f)(5), relating to the definition of a controlled group of corporations
- Section 41(f)(6), regarding an energy research consortium
- Section 41(h), relating to the termination of the federal credit, does not apply for Wisconsin purposes.
- The changes to the federal research credit relating to energy research and energy research consortia were not adopted for Wisconsin purposes.

What Are Qualified Research Expenses

"Qualified research expenses" are defined in Internal Revenue Code section 41(b). 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 as amended to December 31, 2013, for further details.

What Is Qualified Research

"Qualified research" is defined in IRC section 41(d). 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.

Expenses Must Be Incurred in Wisconsin

Expenses incurred entirely outside Wisconsin cannot 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.

Credits Are Income

The credit that you compute on Schedule(s) R is income and must be reported on your Wisconsin franchise or income tax return in the year computed. This is true even if you cannot use the full amount of a credit computed this year to offset tax liability for this year and must carry part or all of it forward to future years.

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 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 must be annualized.

Special Instructions for Combined Group Members

In general, credits are attributes of the separate corporation rather than attributes of the combined group. Nonetheless, s. 71.255(6)(c), Wis. Stats., allows for the sharing of certain research credits. A corporation is not required to share its research credits. Special rules apply to combined group members sharing their respective research credits. Additional information can be found in the instructions to Form 6CS, *Wisconsin Sharing of Research Credits*, and s. Tax 2.61(10)(c) and (d), Wisconsin Administrative Code.

Important features of these special rules include:

- Combined group members compute their respective research credit amounts based on their own "qualified research expenses".
- For combined group members, "qualified research expenses" is modified so that research funded by another combined group member and performed by a different combined group member, is considered qualified research expenses of the combined group member performing the research, and the reimbursement from the combined group member funding the research may not be considered a qualified research expense of the funding member.
- Combined group members use their own respective qualified research expenses for the average of the prior three years qualified research expense computation as if the members themselves filed on a separate entity basis.
- Only the "sharable credits" may be shared. Generally, a corporation may only share its research credits with the combined group if it was a member of that same combined group in the year the credit originated. However, if the credit originated before January 1, 2009, the corporation may share the credit if it would have been in that same combined group had Wisconsin law required combined reporting in the year the credit originated.

Specific Instructions for Schedule R

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.

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

Line 9. On lines 9a through 9c, enter the qualified research expenses for the years indicated. If you did not have qualified research expenses in one or more of the three prior years, check the box on line 9, do not complete lines 9a through 9e, and enter 0 on line 10.

For example, if you had qualified research expenses in 2014 and 2013, but not 2012, do not average your prior year's research expenses. You must use the credit percentage from line 13a, 13b, or 13c.

Line 12. Check the appropriate box to indicate which research credit you are computing. However, if you checked the box on line 9 because you did not have qualified research expenses in one or more of the prior three years, skip line 12 and check the appropriate box on line 13 instead.

Do not check more than one box on line 12. If you qualify to compute more than one research credit, complete a separate Schedule R for each credit.

Line 13. If you checked the box on line 9 because you did not have qualified research expenses in one or more of the three prior years, check the box to indicate which credit you are computing.

Do not check more than one box on line 13. If you qualify to compute more than one research credit, complete a separate Schedule R for each credit.

Line 15. Fill in the amount of research credit passed through from tax-option (S) corporations, partnerships, LLCs treated as partnerships, estates, or trusts. The pass-through credit is shown on Schedule 5K-1 for shareholders of tax-option (S) corporations, Schedule 3K-1 for partners and LLC members, and Schedule 2K-1 for beneficiaries of estates or trusts. Fill in the name, federal employer identification number (FEIN), and amount of credit passed through from the entity. If you were allocated a credit from more than two pass-through entities, attach a schedule showing each entity's name, FEIN, and amount of the credit. Fill in the total pass-through credit from the addition schedule on line 15c and attach the schedule to Schedule R.

Line 16a. *Fiduciaries* – Prorate the credits from line 16 between the entity and its beneficiaries in proportion to the income allocable to each. Show the beneficiaries' portion of the credit on line 16a. Show the credit for each beneficiary on Schedule 2K-1.

Line 16b. Subtract line 16a from line 16. This is the estate’s or trust’s portion of the credit.

Line 17. Enter the research credit from prior taxable years that was not used to offset your tax liability in those years and has not expired under the 15 year carryforward limitation.

Additional Information and Assistance

Web Resources

The Department of Revenue's web page, available at revenue.wi.gov, has a number of resources to provide additional information and assistance, including:

- A home page specifically for combined reporting topics (revenue.wi.gov/combrept/index.html)
- Related forms and their instructions
- Common questions on specific tax topics
- Publications on specific tax topics, including the Wisconsin Research Credit Publication
- The *Wisconsin Tax Bulletin* quarterly publication, which provides information about law changes and other current issues
- Articles addressing administrative issues. A home page specifically for combined reporting topics
- Links to the Wisconsin Statutes and Administrative Code

Contact Information. If you cannot find the answer to your question in the resources available on the Department of Revenue's web page, contact the Department using any of the following methods:

- E-mail your question to: DORFranchise@revenue.wi.gov
- Call (608) 266-2772
  (Telephone help is also available using TTY equipment. Call the Wisconsin Telecommunications Relay System at 711 or, if no answer, (800) 947-3529. These numbers are to be used only when calling with TTY equipment.)
- Send a fax to (608) 267-0834