



**Escaping the Lab, the  
Secrets of Nexus, and More:**  
Timely Tax Topics for Your Business



GAIN OPPORTUNITY:  
RESEARCH & DEVELOPMENT  
CREDIT

# NEW ASPECTS TO RECEIVING R&D CREDITS



Missed prior years?



Develop software?



Beyond the lab

## IN GENERAL...

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### **Standard Method**

IRC Section 41 provides for an income tax credit equal to the sum of 20% of the excess of qualified research expenses (QREs) over a base amount.

### **Alternative Simplified Credit (ASC)**

Under the ASC method, the tax credit equals 14% of the portion of the QREs for the tax year that exceeds 50% of the average QREs for the three tax years preceding the tax year for which the credit is being computed.

# THE ALTERNATIVE SIMPLIFIED CREDIT & AMENDED TAX RETURNS

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## Previous Rule

- Required an election on a timely filed original tax return.
- The election could not be made on an amended tax return.

## New Final Regulations

The regulations remove the rule that prohibits a taxpayer from making the election to use the ASC on an amended return.

## WHAT IS QUALIFIED RESEARCH?

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- Undertaken for the purpose of discovering information
- Technological in nature
- Application intended to be useful in developing a new or improved business component
- Substantially all of the activities of which constitute elements of experimentation for a new or improved function, performance, reliability or quality

# INTERNAL USE SOFTWARE

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## Previous Rule

In order to be qualified research, costs incurred to develop software used internally by a taxpayer had to meet a “high threshold of innovation” test.

- The software must be innovative
- The software development must involve significant risk
- The software must not be commercially available for the taxpayer to use (that is, it is not available without considerable modification)

# INTERNAL USE SOFTWARE

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## New Proposed Regulations

- Provides that *internal use software* is software developed by the taxpayer for use in general and administrative functions that facilitate or support the conduct of the taxpayer's trade or business.
- The proposed regulations provide that software is *not developed primarily for internal use* if it is developed to:
  - be commercially sold, leased, licensed, or otherwise marketed to third parties, or
  - enable a taxpayer to interact with third parties or to allow third parties to initiate functions or review data on the taxpayer's system



# QUALIFYING EXPENSES

- Wages and salaries
- Supplies
- Contract research expenses



## R&D CREDIT

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### Maine

- Activities qualifying for federal R&D credit may qualify for Maine Research Expense credit
- Maine Super Credit for Substantially Increased Research and Development was discontinued



## R&D CREDIT

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### **New Hampshire**

- Credit available for expenditures made during the year for qualified manufacturing R&D
- Application filed by June 30<sup>th</sup>
- Limitations apply (aggregate amount of credit \$2,000,000)





GAIN INSIGHT:  
STATE TAX TOPICS

## STATE TAX TOPICS

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- What is Nexus?
- Apportionment Issues & Trends

## PUBLIC LAW 86-272

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- Restricts a state from collecting income tax where solicitation of sales is the only activity within the state
- Applies only to soliciting sales of tangible personal property
- Protected Activities:

Solicitation of sales by employees or independent contractors if:

- Orders approved outside the state
- Orders filled or shipped from outside the state

# NEXUS

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WHEN DOES NEXUS EXIST?



## PHYSICAL PRESENCE STANDARD

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- Generally, temporary or permanent presence of people (employees, service personnel or sales agents) or property (inventory, offices & warehouses)
- Varies by state



# ECONOMIC NEXUS EXISTS

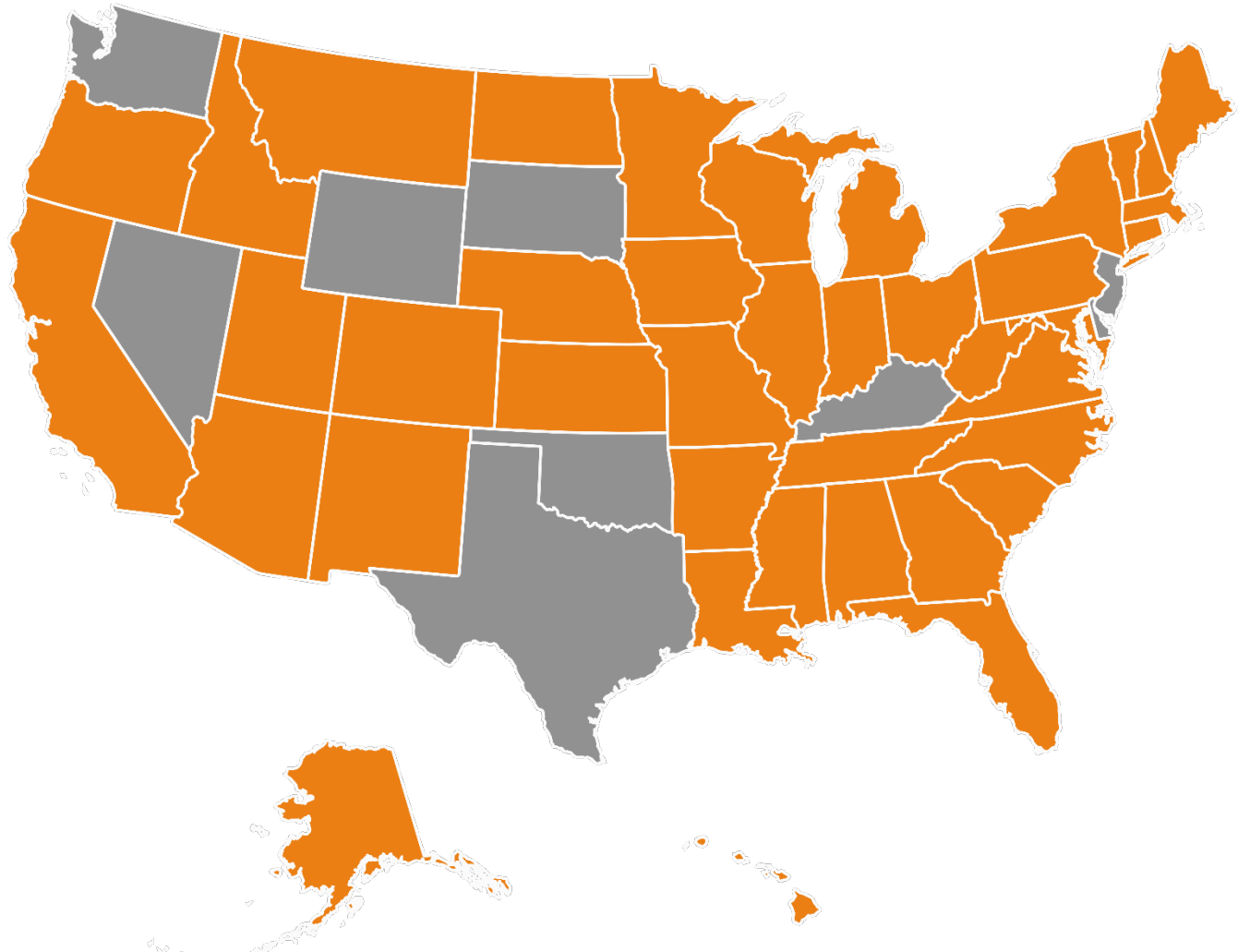
## When an out-of-state business:

- Directs economic activity in the state
- Derives income from a state's local market by making sales to customers in the state
- Receives income from intangible property

## Where there is:

- Affiliation and intercompany transactions
- No affiliation, but direct connections
- No affiliation, but in-state customers

# MOST STATES HAVE ADOPTED ECONOMIC NEXUS STANDARDS



## FACTOR PRESENCE

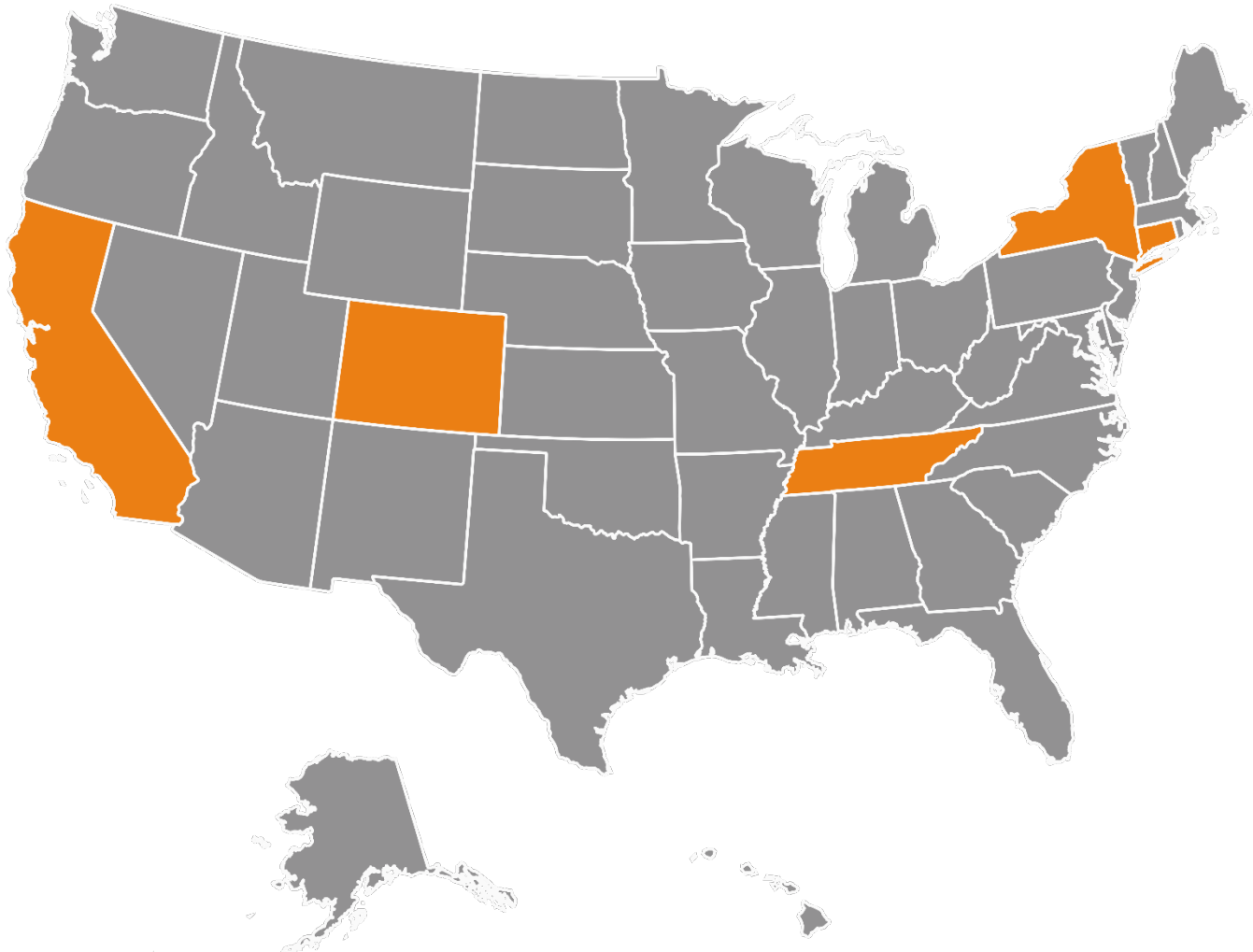
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Multistate Tax Commission standard:

- \$50,000 of property
- \$50,000 of payroll
- \$500,000 of sales
- 25% of total property, total payroll, or total sales

# STATES UTILIZING FACTOR PRESENCE

Income taxes – assuming P.L. 86-272 does not apply



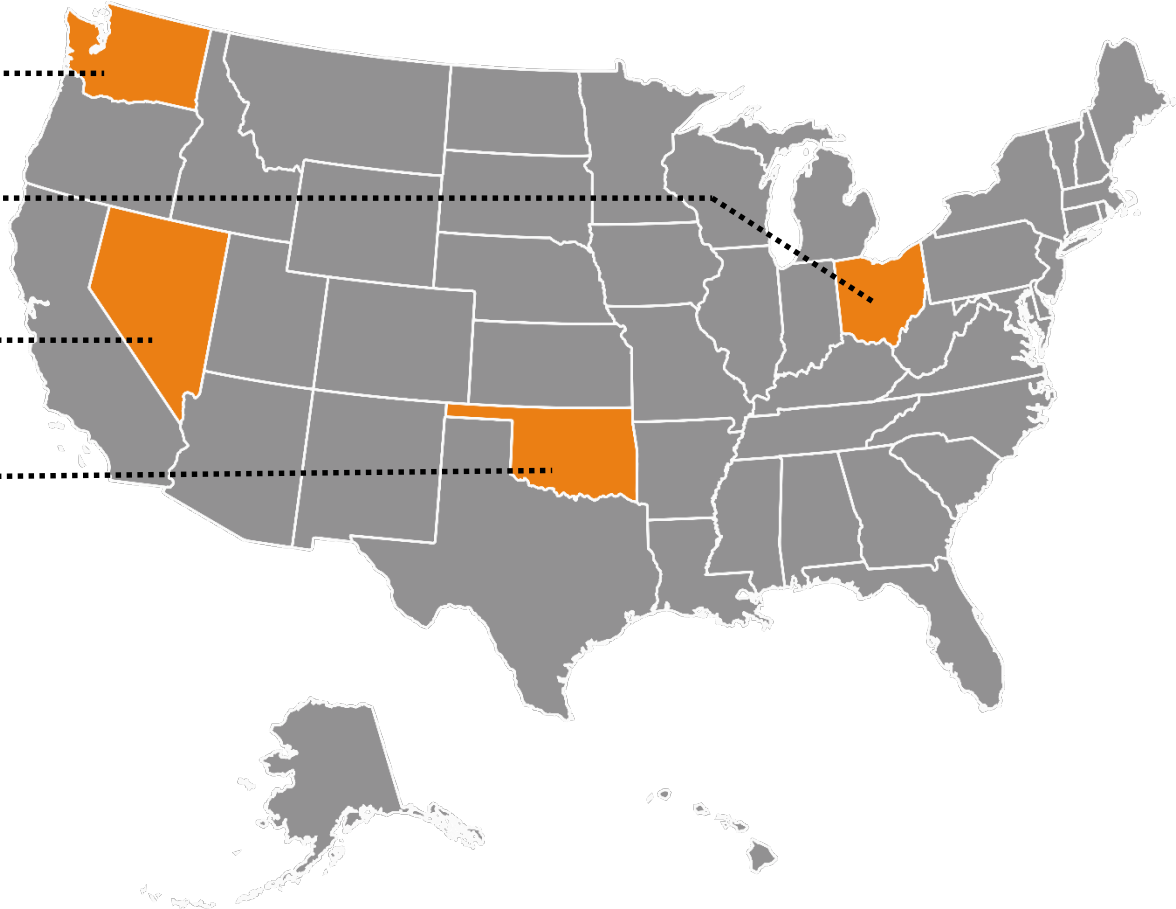
# GROSS RECEIPTS TAXES

Business & Occupancy Tax

Commercial Activity Tax

Commerce Tax

Business Activity Tax



A perspective view of a server room aisle with rows of server racks on both sides. A large, fluffy white cloud is superimposed in the center of the aisle, containing the text for this slide.

## OTHER NEXUS ISSUES

- Web Server Nexus
- Software as a Service (SaaS) or Cloud Computing
- Telecommuting

## CASE STUDY

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Employee of Maine company, working out of home in Missouri, supporting sales function in an engineering capacity

- Sales tax nexus?
- Income tax nexus?

## CASE STUDY

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A Maine manufacturer selling products out-of-state, and contracting with a third-party for installations.


- Sales tax nexus?
- Income tax nexus?



## CALCULATING STATE TAXABLE INCOME

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State tax base



Apportionable business income



Business income



State taxable income

## APPORTIONMENT BASICS

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Computing the apportionment formula

Property factor



Payroll factor



Sales factor

## STATE SPECIFIC APPORTIONMENT METHODS

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- Three factor, equally weighted
- Three factor, double weighted sales factor
- Single sales factor

## SOURCING SALES OF TANGIBLE PROPERTY

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### **Tangible Property:**

Sales of tangible property are generally assigned to the state in which the goods are delivered or shipped.

### **Services:**

- Cost of Performance
- Market-Based

## STATE SPECIFIC SOURCING METHODS

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**MAINE**  
Market-based

**NEW HAMPSHIRE**  
Cost of performance

**VERMONT**  
Cost of performance

**MASSACHUSETTS**  
Market-based

## INTERESTED IN MORE? CONTACT US.

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