

Use Forms 6765 & 8974 to figure payroll tax R&D credit

The IRS has already revised Form 941 to reflect the new research and development tax credit that small employers may take against the employer's share of the Social Security portion of FICA. But there's more to it than claiming the credit on Line 11 of your 941 form.

The picture has now become clearer with the release of revised Form 6765 and new Form 8974 for tax year 2016. *Heads up:* If you're a calendar year taxpayer, you must attach Form 6765 to your business return and file by March 15, 2017.

Background. Small start-up businesses—those with gross receipts of less than \$5 million for the taxable year, and that didn't have gross receipts for the five preceding years, ending with the current taxable year—may take the research and development tax credit against the employer's share of the Social Security portion of FICA taxes, rather than against their income tax liability. The credit is equal to the least of these amounts:

- An amount specified by you, up to \$250,000
- The amount of the research credit determined for the taxable year
- For qualified small businesses other than partnerships or S corporations, the amount of the general business credit carryforward from the taxable year.

Mechanics of making the election. You elect to take the credit by attaching Form 6765, *Credit for Increasing Research Activities*, to your business tax return. The form has been revised to include a new Section D specifically for this purpose. An election made by a partnership or S corp is made at the entity level. *Red flag:* This is only the first step in claiming the credit. If you haven't filed the business tax return making the election on Form 6765, you can't file Form 8974 and you can't claim the credit against your payroll taxes on your 941 form.

The credit is figured on new Form 8974, *Qualified Small Business Payroll Tax Credit for Increasing Research Activities*, which is attached to your 941 form. You can first claim the credit on your 941 for the quarter that begins after you file your income tax return that makes the election on Form 6765.

Example: Mega is a calendar year taxpayer, so it files its 2016 Form 1120 on March 15, 2017. Mega can first claim the credit on its 2017 second quarter 941, which is filed by July 31, 2017.

Unused credits may be carried forward into succeeding quarters until you've used them up.

PAYROLL PRACTICE TIP: The credit can be a valuable source of cash flow to start-up businesses, since they usually have more FICA liability than income tax liability. You should talk this over with your corporate tax people to ensure that you and they are on the same page.