

**DEPARTMENT OF THE TREASURY****Internal Revenue Service****26 CFR Part 1****[REG-130200-08]****RIN 1545-BI09****Election of Reduced Research Credit Under Section 280C(c)(3)****AGENCY:** Internal Revenue Service (IRS), Treasury.**ACTION:** Notice of proposed rulemaking and notice of public hearing.

**SUMMARY:** This document contains proposed regulations that amend the regulations concerning taxpayers who make the election to claim the reduced research credit. The proposed regulations simplify how taxpayers make the election and affect taxpayers that claim the research credit. This document also provides a notice of a public hearing on these proposed regulations.

**DATES:** Written or electronic comments must be received by October 14, 2009. Outlines of topics to be discussed at the public hearing scheduled for November 4, 2009 at 10 a.m. must be received by October 16, 2009.

**ADDRESSES:** Send submissions to: CC:PA:LPD:PR (REG-130200-08), Room 5205, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-130200-08), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC, or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-130200-08). The public hearing will be held in Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

**FOR FURTHER INFORMATION CONTACT:**

Concerning the proposed regulations, David Selig, (202) 622-3040; concerning submission of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Richard A. Hurst, [Richard.A.Hurst@irs.counsel.treas.gov](mailto:Richard.A.Hurst@irs.counsel.treas.gov), (202) 622-7180 (not toll-free numbers).

**SUPPLEMENTARY INFORMATION:****Background and Explanation of Provisions**

This document contains proposed amendments to the Income Tax Regulations (26 CFR Part 1) relating to

the election for claiming the reduced research credit under section 280C(c)(3). Section 280C(c)(1) provides, in general, that no deduction shall be allowed for that portion of the qualified research expenses (as defined in section 41(b)) or basic research expenses (as defined in section 41(e)(2)) otherwise allowable as a deduction for the taxable year which is equal to the amount of the credit determined for such taxable year under section 41(a).

Similarly, section 280C(c)(2) provides that if the amount of the credit determined for the taxable year under section 41(a)(1) exceeds the amount allowable as a deduction for such taxable year for qualified research expenses or basic research expenses (determined without regard to section 280C(c)(1)), the amount chargeable to capital account for the taxable year for such expenses shall be reduced by the amount of such excess.

Section 280C(c)(3)(A) provides, in general, that in the case of any taxable year for which an election is made under section 280C(c)(3), sections 280C(c)(1) and (c)(2) shall not apply, and the amount of the credit under section 41(a) shall be the amount determined under section 280C(c)(3)(B). Under section 280C(c)(3)(B), the amount of credit for any taxable year shall be the amount equal to the excess of the amount of credit determined under section 41(a) without regard to section 280C(c)(3), over the product of the amount of credit determined under section 280C(c)(3)(B)(i), and the maximum rate of tax under section 11(b)(1).

Section 280C(c)(3)(C) provides that an election under section 280C(c)(3) for any taxable year shall be made not later than the time for filing the return of tax for such year (including extensions), shall be made on such return, and shall be made in such manner as the Secretary may prescribe. Such an election, once made, shall be irrevocable.

Section 280C(c)(4) provides that section 280C(b)(3) shall apply for purposes of section 280C(c). Under section 280C(b)(3), in the case of a corporation which is a member of a controlled group of corporations (within the meaning of section 41(f)(5)) or a trade or business which is treated as being under common control with other trades or businesses (within the meaning of section 41(f)(1)(B)), section 280C(b) shall be applied under rules prescribed by the Secretary similar to the rules applicable under section 41(f)(1)(A) and (B).

Currently, § 1.280C-4(a) provides that the section 280C(c)(3) election to have

the provisions of section 280C(c)(1) and (c)(2) not apply shall be made by claiming the reduced credit under section 41(a) determined by the method provided in section 280C(c)(3)(B) on an original return for the taxable year, filed at any time on or before the due date (including extensions) for filing the income tax return for such year. An election, once made, for any taxable year, is irrevocable for that taxable year.

The proposed regulations simplify the section 280C(c)(3) election to have the provisions of section 280C(c)(1) and (c)(2) not apply by requiring the election to be made on Form 6765, "Credit for Increasing Research Activities." The form must be filed with an original return for the taxable year filed on or before the due date (including extensions) for filing the income tax return for such year. An election, once made for any taxable year, is irrevocable for that taxable year.

The IRS and the Treasury Department have received comments on whether all members of a controlled group (as defined in § 1.41-6(a)(3)(ii)) are bound by an election under section 280C(c)(3), or whether each member of a controlled group can make a separate election under section 280C(c)(3). If a taxpayer is a member of a controlled group, section 280C(c)(4) requires that the election for the reduced research credit must be determined under rules similar to rules applicable to a controlled group. Section 1.41-6(a)(1) provides that to determine the amount of research credit (if any) allowable to a trade or business that at the end of its taxable year is a member of a controlled group, a taxpayer must: (i) compute the group credit in the manner described in § 1.41-6(b), and (ii) allocate the group credit among the members of the group in the manner described under § 1.41-6(c). All members of the controlled group are required to use the same computation method, that is, the section 41(a)(1) method, the section 41(c)(4) alternative incremental research credit (alternative incremental credit) method, or the section 41(c)(5) alternative simplified research credit method, in computing the group credit for the credit year. Under section 41(h)(2), as amended by section 301(b) of the Tax Extenders and Alternative Minimum Tax Relief Act of 2008 (Div. C of Public Law 110-343, 122 Stat. 3765), a taxpayer cannot elect the alternative incremental research credit under section 41(c)(4) for taxable years beginning after December 31, 2008.

The reduced research credit under section 280C(c)(3) is not a computational rule under section 41 used for computing the group credit for a credit year under §§ 1.41-6(b)(1) and

1.41–6T(b)(1). There is no change to the overall tax effect of the research credit if each member of a controlled group, after computing and allocating its share of the group credit under §§ 1.41–6(b)(1) and 1.41–6(c) and 1.41–6T(b)(1) and 1.41–6(c)(2), determines whether it wants to claim the reduced research credit under section 280C(c)(3)(B). Accordingly, the proposed regulations provide that each member of a controlled group may make the election under section 280C(c)(3) after the group credit is computed and allocated under §§ 1.41–6(b)(1) and 1.41–6(c) and 1.41–6T(b)(1) and 1.41–6T(c)(2).

#### Proposed Effective Date

The regulations are proposed to apply to taxable years ending on or after the date of publication of the Treasury decision adopting these rules as final regulation in the **Federal Register**.

#### Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations.

When an agency issues a rulemaking proposal, the Regulatory Flexibility Act (5 U.S.C. chapter 6), requires the agency to “prepare and make available for public comment an initial regulatory flexibility analysis” that will “describe the impact of the proposed rule on small entities.” (5 U.S.C. 603(a)). Section 605 of the Regulatory Flexibility Act provides an exception to this requirement if the agency certifies that the proposed rulemaking will not have a significant economic impact on a substantial number of small entities.

The proposed rule affects individuals and small businesses engaged in research activities under section 41. The IRS has determined that this proposed rule will have an impact on a substantial number of small entities. However, the IRS also has determined that the impact on entities affected by the proposed rule will not be significant. This determination is based on the fact that the regulations would simplify the procedure for making the election for the reduced research credit under section 280C(c)(3)(C). Instead of requiring such an election to be made “on an original return,” the regulations specify that the election is made on Form 6765, “Credit for Increasing Research Activities,” which is attached to the return. This form requires only a minimal amount of time to complete

and places no greater burden on the taxpayer than the current procedure. Accordingly, a Regulatory Flexibility Analysis is not required.

Pursuant to section 7805(f) of the Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

#### Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and the Treasury Department request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying.

A public hearing has been scheduled for November 4, 2009, at 10 a.m. in Auditorium of the Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. Due to building security procedures, visitors must enter at the Constitution Avenue entrance. In addition, all visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the **FOR FURTHER INFORMATION CONTACT** section of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments at the hearing must submit electronic or written comments and an outline of the topics to be discussed and the time to be devoted to each topic (a signed original and eight (8) copies) by October 16, 2009. A period of 10 minutes will be allotted to each person for making comments. An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

#### Drafting Information

The principal author of these regulations is David Selig, Office of Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and the Treasury Department participated in their development.

#### List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

#### Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

#### PART 1—INCOME TAXES

**Paragraph 1.** The authority citation for part 1 continues to read in part as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

**Par. 2.** Section 1.280C–4 is revised to read as follows:

#### § 1.280C–4 Credit for increasing research activities.

(a) *In general.* An election under section 280C(c)(3) to have the provisions of section 280C(c)(1) and (c)(2) not apply and elect the reduced research credit under section 280C(c)(3)(B) shall be made on Form 6765, “Credit for Increasing Research Activities,” (or any successor form). In order for the election to be effective, the Form 6765 must clearly indicate the taxpayer’s intent to make the section 280C(c)(3) election, and must be filed with an original return for the taxable year filed on or before the due date (including extensions) for filing the income tax return for such year, regardless of whether any research credits are claimed on the original return. An election, once made for any taxable year, is irrevocable for that taxable year.

(b) *Controlled groups of corporations; trades or businesses under common control.* A member of a controlled group of corporations (within the meaning of section 41(f)(5)), or a trade or business which is treated as being under common control with other trades or businesses (within the meaning of section 41(f)(1)(B)), may make the election under section 280C(c)(3). Such member or trade or business shall make the election on Form 6765 and by the time prescribed in paragraph (a) of this section.

(c) *Effective/applicability date.* This section applies to taxable years ending on or after the date of publication of the Treasury Decision adopting these rules as final regulations in the **Federal Register**.

**Linda E. Stiff,**

*Deputy Commissioner for Services and Enforcement.*

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