

BILL ANALYSIS

S.B. 2206
By: Bettencourt
Ways & Means
Committee Report (Unamended)

BACKGROUND AND PURPOSE

The bill sponsor has informed the committee that research and development (R&D) activities can create high-paying jobs, provide substantial benefits to the Texas economy, produce new technologies and applications that generate economic efficiency and growth, and accelerate partnerships with institutions of higher education that expand opportunities for innovation and learning and that, for these reasons, state governments often attempt to encourage the expansion of R&D projects in their states. Under current state law, taxpayers can claim either a franchise tax credit for certain R&D activities or a sales and use tax exemption for certain property used in R&D activities, similar to the federal income tax credit for certain research activities. However, the state's franchise tax credit for certain R&D activities is set to expire December 31, 2026. S.B. 2206 seeks to keep Texas economically competitive in the field of R&D and encourage new investments in Texas by extending the franchise tax credit beyond that expiration date and by making the administration of the credit more efficient for both taxpayers and the comptroller of public accounts.

CRIMINAL JUSTICE IMPACT

It is the committee's opinion that this bill does not expressly create a criminal offense, increase the punishment for an existing criminal offense or category of offenses, or change the eligibility of a person for community supervision, parole, or mandatory supervision.

RULEMAKING AUTHORITY

It is the committee's opinion that rulemaking authority is expressly granted to the comptroller of public accounts in SECTION 1 of this bill.

ANALYSIS

Franchise Tax Credit

S.B. 2206 amends the Tax Code, effective January 1, 2026, to provide for a franchise tax credit for certain research and development expenses and repeals existing Tax Code provisions relating to a franchise tax credit for certain research and development activities that are set to expire December 31, 2026.

Definition

S.B. 2206 defines "public or private institution of higher education" for purposes of the bill's provisions relating to the franchise tax credit for certain research and development activities as:

- a public institution of higher education, as defined by the Higher Education Coordinating Act of 1965; or
- a private or independent institution of higher education, as defined by that act.

Qualified Research Expense

S.B. 2206 defines "qualified research expense," for purposes of the bill's provisions relating to the franchise tax credit for certain research and development activities, as, subject to these provisions, the portion of the amount reported by a taxable entity as the entity's total qualified research expenses on line 48 of Form 6765, that is attributable to research conducted in Texas, excluding any amount that is not paid or incurred by the taxable entity, a member of the entity's combined group, or a lower tier entity as provided by the bill's provisions relating to combined reporting. The bill establishes the following for purposes of these provisions:

- a reference to Form 6765 is a reference to IRS Form 6765 and includes a revised version of that form or a subsequent form with a different number or designation that substantially provides the same information as Form 6765; and
- a reference to a line number on Form 6765 includes a different line number on a revised or subsequent form that substantially provides the same information as the line number originally referenced.

The bill also establishes, for purposes of these provisions, that a reference to an amount reported on a line number on Form 6765 is:

- generally, a reference to the amount entered on that line number to the extent the amount entered complies with federal law in effect for the federal tax year for which the form is filed with the IRS;
- if an amended Form 6765 is filed by the taxable entity with the IRS before the expiration of the period for claiming a refund of federal income tax for the federal tax year for which the amended form is filed, a reference to the amount entered on that line number on the amended form; or
- if the IRS has audited the federal income tax return of a taxable entity for a federal tax year for which the taxable entity filed Form 6765 with the IRS and the audit has been made final, a reference to the amount reported on that line number on the form as audited or adjusted by the IRS.

For purposes of determining the amount on line 48 of Form 6765 under these provisions:

- a taxable entity or the comptroller of public accounts may use statistical sampling procedures if the procedures are permitted by the IRS's Revenue Procedure 2011-42 or a successor publication issued by the IRS; and
- expenses for supplies properly reportable by a taxable entity as qualified research expenses on either of those lines may not be excluded from the computation of those expenses for purposes of the bill's provisions on the basis that the supplies are taxable, nontaxable, or exempted from taxation under the Limited Sales, Excise, and Use Tax Act.

If the IRS or the comptroller determines that a taxable entity has satisfied the requirements of the IRS to accept as sufficient evidence of the entity's qualified research expenses the entity's adjusted Accounting Standards Codification 730 financial statement research and development costs for a federal tax credit year, then the portion of those adjusted costs that is related to research conducted in Texas is sufficient evidence of the entity's qualified research expenses for that federal tax credit year for purposes of the franchise tax credit under the bill's provisions.

Eligibility for Credit

S.B. 2206 makes a taxable entity eligible for a franchise tax credit in the amount and under the conditions provided by the bill's provisions.

Amount of Credit

S.B. 2206 establishes the following with respect to the amount of the credit:

- generally, the credit for any report equals 8.722 percent of the difference between the following:
 - the qualified research expenses incurred during the period on which the report is based; and

- 50 percent of the average amount of qualified research expenses incurred during the three tax periods preceding the period on which the report is based;
- if the taxable entity contracts with one or more public or private institutions of higher education and the entity incurs qualified research expenses under the contract during the period on which the report is based, the credit for the report equals 10.903 percent of the difference between the following:
 - all qualified research expenses incurred during the period on which the report is based; and
 - 50 percent of the average amount of all qualified research expenses incurred during the three tax periods preceding the period on which the report is based;
- if the taxable entity has no qualified research expenses in one or more of the three tax periods preceding the period on which the report is based, the credit for the period on which the report is based equals 4.361 percent of the qualified research expenses incurred during that period; and
- if the taxable entity contracts with one or more public or private institutions of higher education and the entity incurs qualified research expenses under the contract during the period on which the report is based, but has no qualified research expenses in one or more of the three tax periods preceding the period on which the report is based, the credit for the period on which the report is based equals 5.451 percent of all qualified research expenses incurred during that period.

S.B. 2206 establishes that, notwithstanding whether the time for claiming a credit under the bill's provisions has expired for any tax period used in determining the average amount of qualified research expenses incurred during the three tax periods preceding the period on which the report is based, the determination of which research expenses are qualified research expenses for purposes of computing that average must be made in the same manner as that determination is made for purposes of calculating the qualified research expenses incurred during the period on which the report is based. This provision does not apply to a credit to which a taxable entity was entitled under repealed Tax Code provisions providing for a franchise tax credit for qualified research activities as those provisions existed before January 1, 2008.

S.B. 2206 authorizes the comptroller to adopt rules for determining which research expenses are qualified research expenses for purposes of calculating the amount of the credit generally or if an applicable taxable entity contracts with one or more public or private institutions of higher education and the entity incurs qualified research expenses under the contract during the period on which the report is based to prevent disparities in those determinations that may result from the taxable entity using different accounting methods for the period on which the report is based, as compared to any preceding tax periods used in determining the average amount of qualified research expenses incurred during the three tax periods preceding the period on which the report is based.

Credit for Certain Taxable Entities That Owe No Tax

S.B. 2206 authorizes a taxable entity that incurs qualified research expenses during a period for which the entity is not required to pay the franchise tax for any of the following reasons to calculate the amount of the credit to which the entity would otherwise be entitled under the bill's provisions on a report and receive that amount as a refundable credit:

- the taxable entity qualifies as a new veteran-owned business;
- the amount of tax computed for the taxable entity is less than \$1,000; or
- the amount of the taxable entity's total revenue from its entire business is less than or equal to \$2.47 million or the applicable adjusted amount based on the percentage increase or decrease during the preceding state fiscal biennium in the consumer price index per 12-month period on which margin is based.

In determining the amount of the credit that may be refunded to a taxable entity under these provisions, the limitation on the total amount of credit claimed under the bill's provisions for a report prescribed by the bill does not apply.

S.B. 2206 requires a taxable entity to apply for a credit under the bill's provisions on or with the report for the period for which the credit is claimed or, if the entity does not file a report for the applicable period, on a form adopted by the comptroller. The bill requires the form to be submitted to the comptroller on or before the date a report for the period for which the credit is claimed would be due.

Combined Reporting

S.B. 2206 requires a credit under the bill's provisions for qualified research expenses incurred by a member of a combined group to be claimed on the combined report required by applicable state law for the group and establishes that the combined group is the taxable entity for purposes of the bill's provisions. The bill authorizes an upper tier entity that includes the total revenue of a lower tier entity for purposes of computing its taxable margin as authorized by provisions relating to reporting for certain partnerships in a tiered partnership arrangement to claim the credit under the bill's provisions for qualified research expenses incurred by the lower tier entity to the extent of the upper tier entity's ownership interest in the lower tier entity.

Limitation

S.B. 2206 caps the amount of the total credit claimed under the bill's provisions for the report, including the amount of any carryforward under the bill's provisions, at an amount not to exceed 50 percent of the amount of tax due for the report before any other applicable tax credits.

Carryforward

S.B. 2206 authorizes a taxable entity, if the taxable entity is eligible for a credit that exceeds the limitation under the bill's provisions, to carry the unused credit forward for not more than 20 consecutive reports. Credits, including credit carryforwards, are considered used in the following order:

- a credit carryforward of unused credits accrued under repealed Tax Code provisions providing for a franchise tax credit for qualified research activities before the repeal of those provisions on January 1, 2008, and claimed as authorized by Chapter 1 (H.B. 3), Acts of the 79th Legislature, 3rd Called Session, 2006;
- a credit carryforward of unused credits accrued under existing Tax Code provisions, which are set to expire December 31, 2026, providing for a franchise tax credit for certain research and development activities before the repeal of those provisions on January 1, 2026, and claimed as authorized by applicable legislation;
- a credit carryforward under the bill's provisions; and
- a current year credit.

Assignment Prohibited

S.B. 2206 prohibits a taxable entity from conveying, assigning, or transferring the credit allowed under the bill's provisions to another entity unless substantially all of the assets of the taxable entity are conveyed, assigned, or transferred in the same transaction.

Application for Credit

S.B. 2206 requires a taxable entity, except as otherwise provided by the bill's provisions, to apply for a credit under the bill's provisions on or with the report for the period for which the credit is claimed.

Rules

S.B. 2206 authorizes the comptroller to adopt rules and forms necessary to implement the bill's provisions.

Reporting of Estimates

S.B. 2206 requires the comptroller, before the beginning of each regular session of the legislature, to submit to the legislature and the governor estimates of the following:

- the total number of taxable entities that applied credits under the bill's provisions against the franchise tax or received refundable credits under the bill's provisions;
- the total amount of those credits and refundable credits; and
- the total amount of unused credits carried forward.

The bill requires the comptroller to provide the required estimates as part of the biennial report submitted by the comptroller to the legislature and the governor on the effect of certain tax provisions.

Deposit of Certain Revenue

S.B. 2206 requires the comptroller, for each state fiscal year, to deposit to the credit of the property tax relief fund an amount of revenue received from the franchise tax sufficient to offset any decrease in deposits to that fund for the state fiscal year that results from the implementation of the bill's provisions.

Report of Changes to Federal Income Tax Return

S.B. 2206 requires a taxable entity to file an amended report under statutory provisions relating to the franchise tax if:

- the amount of qualified research expenses incurred by the taxable entity is changed as the result of an audit or other adjustment by the IRS or another competent authority; or
- the taxable entity files an amended federal income tax return or other return that changes the amount of qualified research expenses incurred by the taxable entity.

For these purposes, the bill establishes that the term "qualified research expense" has the same meaning assigned by the bill's provisions relating to the franchise tax credit for certain research and development activities.

Repealed Provisions

S.B. 2206 repeals the following provisions that are set to expire December 31, 2026:

- Section 151.3182, Tax Code, which provides for a sales and use tax exemption for certain property used in research and development activities; and
- Subchapter M, Chapter 171, Tax Code, which provides for a franchise tax credit for certain research and development activities.

The bill establishes the following with respect to the repeal of those provisions:

- the repeal of Section 151.3182, Tax Code, does not affect tax liability accruing before the bill's effective date and that liability continues in effect as if those provisions had not been repealed, and the former law is continued in effect for the collection of taxes due and for civil and criminal enforcement of the liability for those taxes; and
- the repeal of Subchapter M, Chapter 171, Tax Code, does not affect an unused credit a taxable entity was authorized to carry forward under those provisions and a taxable entity may continue to apply those credits on or with each consecutive report until the date the credit would have expired under those provisions, had those provisions continued in effect, and the former law under which the taxable entity accrued the credits is continued in effect for purposes of determining the amount of the credits the taxable entity may claim and the manner in which the taxable entity may claim the credits.

Applicability

S.B. 2206 applies only to a report originally due on or after the bill's effective date. A taxable entity is not eligible for and may not claim on a report a credit under the bill's provisions if the taxable entity, or a member of the taxable entity's combined group if the taxable entity is a combined group, received a sales and use tax exemption for certain property used in research and development activities during the period for which the report is based.

EFFECTIVE DATE

January 1, 2026.