



Bulletin

2007-02B

LOCAL OPTION EXEMPTION FOR RESEARCH AND DEVELOPMENT

TO: Assessors, Mayors, Selectmen, City/Town Managers, Finance Directors and Clerks

FROM: Gerard D. Perry, Deputy Commissioner, Division of Local Services

DATE: February 2007

SUBJECT: New Local Option Property Tax Exemptions for Research & Development Companies

This *Bulletin* explains sections of the 2006 Economic Stimulus Act that create local option personal property tax exemptions for research and development (R&D) corporations and some limited liability companies (LLCs) engaged in R&D. Once accepted, the provisions effectively treat these R&D companies as manufacturing corporations for local property tax purposes. St. 2006, c. 123, §§42-47, amending G.L. c. 59, §5, Clauses 16 and 16A. The *Bulletin* also requires that local acceptance of the new exemptions be reported to the Division of Local Services.

These economic stimulus act sections:

- Allow cities and towns, by accepting local option provisions, to grant significant personal property tax exemptions to (1) R&D corporations and (2) certain limited liability companies engaged in R&D that existed and conducted business in Massachusetts on or before January 15, 1996.
- Require boards of assessors in communities that accept the local option provisions to follow the Commissioner of Revenue's classification of a corporation or limited liability company as R&D.

These local option provisions become operative in a community for a fiscal year only if accepted by the community before the January 1 assessment date for that year.

If you have questions, please contact the Bureau of Municipal Finance Law at 617-626-2400.

LOCAL OPTION EXEMPTION FOR RESEARCH AND DEVELOPMENT
Chapter 123, §§42-47 of the Acts of 2006
Amending General Laws Chapter 59, §5, Clauses 16 and 16A

Research and Development Exemption

This act creates two separate local option personal property tax exemptions for (1) research and development (R&D) corporations and (2) specially defined limited liability companies (LLCs) engaged in R&D. The provisions amend G.L. c. 59, §5, cl. 16(3) and (5) and cl. 16A, which currently provide extensive personal property tax exemptions to corporations and specifically defined LLCs that are classified as manufacturing by the Commissioner of Revenue. Before these amendments, R&D corporations had to be classified as manufacturing to receive personal property tax exemptions. The new exemptions must be accepted before the January 1 assessment date for a fiscal year in order to apply for that year. A city or town may accept either exemption, or both exemptions.

The new R&D personal property tax exemptions are the same as those for classified manufacturing corporations. If accepted, qualifying corporations and LLCs will be assessed personal property tax only on poles, wires, underground conduits and pipes. They will not be taxable on other personal property. Ordinarily, R&D corporations are taxable on machinery used in the conduct of business. LLCs engaged in R&D are usually taxable on all personal property or, if the LLC qualifies to be treated as a corporation based on its federal income tax election, machinery used in the conduct of business.

Research and development includes experimental or laboratory activity having as its ultimate goal the development of new products, the improvement of existing products, the development of new uses for existing products and the development or improvement of methods for producing products. It does not include testing or inspection for quality control purposes, efficiency surveys, management studies, consumer surveys or other market research, advertising or promotional activities or research in connection with literacy, historical or similar projects. Research and development corporations must derive more than two-thirds of their receipts, or incur more than two-thirds of their expenditures, attributable to Massachusetts from R&D activity during the taxable year. In determining the amount of R&D activity of a company, all its manufacturing expenditures are excluded from the total, whether or not the manufacturing activity is substantial. Receipts from R&D include those from R&D services, royalties or fees from the licensing of patents, know-how or other technology developed from R&D. See G.L. c. 63, §§38C and 42B, which define manufacturing and R&D corporations under G.L. c. 59, §5, cl. 16(3).

The corporate R&D exemption applies to classified R&D corporations only in communities that accept the R&D exemption provision of G.L. c. 59, §5, cl. 16(3). St. 2006, c. 123, §46. If accepted, the corporate R&D exemption will also apply to those classified R&D LLCs that are treated as corporations for corporate excise and personal property tax purposes, *i.e.* those that elect to file their federal returns as corporations.

Under local option G.L. c. 59, §5, cl. 16A, other LLCs may qualify for manufacturing classification and the manufacturing corporation personal property tax exemption, even if they are not ordinarily considered corporations. In communities that accept Clause 16A, these LLCs will also qualify for R&D classification and the R&D corporation personal property tax exemption. To qualify for manufacturing and R&D exemptions under Clause 16A, LLCs must (1) be wholly owned by corporations, (2) be engaged in R&D in Massachusetts, and (3) have been in existence and conducting business in Massachusetts on or before January 15, 1996.

Acceptance Procedures

Acceptance of the R&D exemption for corporations and LLCs treated as corporations under G.L. c. 59, §5, cl. 16(3) is by majority vote of the municipal legislative body, subject to local charter. G.L. c. 4, §4.

Cities and towns that have already accepted G.L. c. 59, §5, cl. 16A do not need to take any further action. The R&D exemption for qualifying LLCs will be effective in those communities beginning in fiscal year 2008. Communities that have not accepted clause 16A may do so by majority vote of the municipal legislative body, subject to local charter. In those communities, both the R&D and manufacturing exemptions will apply to qualifying LLCs.

The exemption applies to personal property assessments as of the January 1 following the acceptance vote. For example, an acceptance voted after January 1, 2007 and before January 1, 2008 would be effective for taxes assessed as of January 1, 2008 for fiscal year 2009.

Classification of R&D Companies

The Commissioner does not currently classify R&D corporations or LLCs treated as corporations. These companies need only check a box on their state corporate excise returns to seek state tax benefits. However, for those communities that accept or plan to accept the new R&D exemptions, the Commissioner will develop procedures to classify qualifying companies in the community on a case-by-case basis.

Notification Requirements

The city or town clerk must notify the Municipal Data Management/Technical Assistance Bureau if either R&D exemption is accepted. (See attached "Notification of Acceptance"). The notice should be submitted within 30 days of acceptance. If the community has already accepted Clause 16A, the notice should be submitted as soon as possible. As explained above, these notices will assist the Commissioner determine if new procedures must be developed to classify companies engaged in R&D in the community.

(City/Town)

NOTIFICATION OF ACCEPTANCE
General Laws Chapter 59, §5, Clauses 16 and 16A
(Research and Development Corporations/LLCs Personal Property Tax Exemption)

The Commissioner of Revenue is hereby notified that the City/Town of _____, by action of its legislative body on _____, _____, has accepted Clause 16(3) of General Laws Chapter 59, Section 5 regarding the taxation of research and development corporations, effective beginning in fiscal year _____.

The Commissioner of Revenue is hereby notified that the City/Town of _____, by action of its legislative body on _____, _____, has accepted Clause 16A of General Laws Chapter 59, Section 5 regarding the taxation of certain research and development limited liability companies, effective beginning in fiscal year _____.

(City/Town Clerk)

(Date)

PLEASE ATTACH A CERTIFIED COPY OF EACH VOTE AND SUBMIT TO:

Municipal Data Management/Technical Assistance Bureau
Division of Local Services
P.O. Box 9569
Boston, MA 02114-9569