

# Instructions for Form 8974 (January 2017)



Department of the Treasury  
Internal Revenue Service

## Qualified Small Business Payroll Tax Credit for Increasing Research Activities

Section references are to the Internal Revenue Code unless otherwise noted.

### Future Developments

For the latest information about developments related to Form 8974 and its instructions, such as legislation enacted after they were published, go to [IRS.gov/form8974](http://IRS.gov/form8974).

## General Instructions

### Purpose of Form 8974

Use Form 8974 to determine the amount of the qualified small business payroll tax credit for increasing research activities that you can claim on Form 941, Employer's QUARTERLY Federal Tax Return; Form 941-SS, Employer's QUARTERLY Federal Tax Return (American Samoa, Guam, the Commonwealth of the Northern Mariana Islands, and the U.S. Virgin Islands); or Form 941-PR, Planilla para la Declaración Federal TRIMESTRAL del Patrono. This payroll tax credit is a credit against the employer portion of social security tax on the wages of your employees.

All references to Form 941 in these instructions also apply to Forms 941-SS and 941-PR.

**Form 943 and Form 944 filers.** If you file Form 943, Employer's Annual Federal Tax Return for Agricultural Employees, or Form 944, Employer's ANNUAL Federal Tax Return, Form 8974 and these instructions will be revised at the end of 2017 to provide instructions for you to claim the credit.

### Who Must File Form 8974?

You must file Form 8974 and attach it to Form 941 if you made an election on your income tax return to take a portion of the qualified small business payroll tax credit for increasing research activities against your payroll taxes. The election is made on Form 6765, Credit for Increasing Research Activities. If you haven't filed the income tax return making the election to claim the payroll tax credit on Form 6765, you can't file Form 8974 and can't claim the qualified small business payroll tax credit for increasing research activities against your payroll taxes on Form 941.



*You can't claim the qualified small business payroll tax credit for increasing research activities on a Form 941 unless you make the election on Form 6765 and file Form 8974 and attach it to Form 941.*

### Aggregate Form 941

If you're a Section 3504 agent or a Certified Professional Employer Organization (CPEO), you must complete Schedule R (Form 941), Allocation Schedule for Aggregate Form 941 Filers, when filing an aggregate Form 941. Additionally, you must attach a Form 8974 for

each client that is taking the qualified small business payroll tax credit for increasing research activities. See the instructions for line 8 and line 9, later, for more information.

### Correcting Form 8974

If you discover an error on a previously filed Form 8974, make the correction by filing Form 941-X, Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund, with a corrected Form 8974. For more information, see the Instructions for Form 941-X.

### When Must You File?

Form 8974 is filed with Form 941. You can first claim the qualified small business payroll tax credit for increasing research activities on the Form 941 for the quarter that begins after you file your income tax return that makes the election on Form 6765. The Form 941 for that quarter is the Form 941 on which you are required to claim the qualified small business payroll tax credit for increasing research activities for the amount elected as a research payroll tax credit on Form 6765. You can't claim the credit related to this election on a different quarter's Form 941 unless it is to take a carryforward credit from the required quarter, as determined on Form 8974.

**Example.** If you file your 2016 income tax return based on a calendar year (January 1–December 31) on March 15, 2017, the 2017 second quarter (April 1, 2017–June 30, 2017) Form 941, which is filed by July 31, 2017, is the first quarter that you can take the qualified small business payroll tax credit for increasing research activities.

## Specific Instructions

### Enter Your Business Information

Enter your employer identification number (EIN) and name at the top of Form 8974. Make sure that they exactly match the name of your business and the EIN that the IRS assigned to your business and also match the name and EIN shown on Form 941. Also check a box to tell us on which form you'll take the credit from Part 2, line 12.

### Calendar Year

Enter the calendar year as shown on the attached Form 941.

### Check the Box for the Quarter

Under *Report for this quarter* at the top of Form 8974, check the appropriate box of the quarter for which you're filing Form 8974. The quarter must match the quarter as shown on Form 941.

## Part 1: Tell Us About Your Income Tax Return

### Line 1

Tell us which income tax return you filed that elected a qualified small business payroll tax credit on Form 6765. Form 6765 can only be attached to Form 1040, 1065, 1120, 1120-F, or 1120S.

### Line 2

Tell us which tax period was covered by the income tax return shown on line 1. If your income tax return was for a calendar year, enter the year as “YYYY” (for example, 2016). If your income tax return was for a fiscal year, enter the date the tax year began and ended as “MM/DD/YYYY” (for example, tax year beginning 07/01/2016 ending 06/30/2017).

### Line 3

Tell us the date that you filed your income tax return that is shown on line 1. Enter the date as “MM/DD/YYYY” (for example, 03/15/2017).

### Line 4

If the EIN used on Form 8974 isn't the same as the EIN used on Form 6765, enter the EIN that was used on Form 6765. Generally, the EIN used on Form 8974 should be the same as the EIN used on Form 6765. However, if you're a member of a controlled group of corporations (as defined in section 41(f)(1)(A) and (f)(5)) or a member of a group of trades or businesses under common control (as defined in section 41(f)(1)(B) and Regulations section 1.41-6(a)(3)(ii)), the EIN used on Form 6765 may be different from the EIN that you must use on Form 8974.

## Part 2: Determine the Credit That You Can Use This Period

### Line 5

Generally, enter the amount from Form 6765, line 44. However, if you're a member of a controlled group of corporations (as defined in section 41(f)(1)(A) and (f)(5)) or a member of a group of trades or businesses under common control (as defined in section 41(f)(1)(B) and Regulations section 1.41-6(a)(3)(ii)), enter the amount of the credit that was allocated to your EIN. As a member, your credit is determined on a proportionate basis to your share of the aggregate qualified research expenses for increasing research activities taken into account by the group for the research credit.

### Line 6

Enter the amount of the credit from line 5 that was taken in a previous period or previous periods.

**Carryforward.** If the qualified small business payroll tax credit for increasing research activities reported on line 5 can't be fully used in the first quarter after the income tax return is filed, you can carryforward any unused amount to the next quarter. If, in the next quarter the amount carried over from the first quarter can't be fully used because of the limit to the employer social security tax on wages for

that quarter (the next quarter), then you can carryforward any unused amount to the quarter after the next quarter. For subsequent quarters, if the qualified small business payroll tax credit for increasing research activities on line 7 can't be fully used in the quarter, you can carryforward any unused amount to the following quarter.

**Example.** You elected to take \$100,000 as a qualified small business payroll tax credit for increasing research activities when you filed your 2016 income tax return on March 15, 2017. On the Form 8974 that you attach to your second quarter 2017 Form 941, you enter \$100,000 on line 5 and leave line 6 blank because the second quarter of 2017 is the first time you're using the elected amount from your 2016 income tax return. You complete lines 7–12 and learn that you can only use \$75,000 of the credit for the second quarter of 2017. You have a \$25,000 carryforward to the third quarter of 2017.

On the Form 8974 that you attach to your third quarter 2017 Form 941, you will complete Part 1 with the same information (your 2016 income tax return information) that you reported for the second quarter of 2017. You will enter \$100,000 on line 5 (same as you did for the second quarter of 2017) but you now must also enter \$75,000 on line 6 because this is the amount of the credit on line 5 that you claimed in a previous period.

### Line 7

Subtract line 6 from line 5. Enter the result on line 7.

### Line 8

Enter the amount from Form 941, line 5a, column 2. This is the total amount of social security tax on wages.



*If you're filing an aggregate Form 941, you must prepare a Form 8974 for each client that is taking the qualified small business payroll tax credit for increasing research activities. Also, you can't enter the amount from Form 941, line 5a, column 2, on line 8 of any of the Forms 8974 that are attached to the aggregate Form 941. The credit is based on each employer's liability for social security tax. Therefore, you must enter on line 8 of each client's Form 8974 the amount that the client would've reported on Form 941, line 5a, column 2, if the client filed its own Form 941.*

### Line 9

Enter the amount from Form 941, line 5b, column 2. This is the total amount of social security tax on tips for the quarter.



*If you're filing an aggregate Form 941, you must prepare a Form 8974 for each client that is taking the qualified small business payroll tax credit for increasing research activities. Also, you can't enter the amount from Form 941, line 5b, column 2, on line 9 of any of the Forms 8974 that are attached to the aggregate Form 941. The credit is based on each employer's liability for social security tax. Therefore, you must enter on line 9 of each client's Form 8974 the amount that the client would've reported on Form 941, line 5b, column 2, if the client filed its own Form 941.*

## Line 10

Add lines 8 and 9. Enter the result on line 10.

## Line 11

Multiply line 10 by 50% (0.50). The qualified small business payroll tax credit for increasing research activities can only be used against the employer's share of social security tax reported on Form 941. The amount on line 10 is the total amount of social security tax (both the employer and employee share) so you must multiply line 10 by 50% to limit the credit to the employer's share of social security tax. See the instructions below if you are a third-party payer of sick pay or you received a Section 3121(q) Notice and Demand.

### Third-Party Payers of Sick pay

You can only take the qualified small business payroll tax credit for increasing research activities against the employer's share of social security tax on wages paid to your employees. Because the amount entered on line 8 included social security tax for your clients' employees, you must make an adjustment to the amount reported on line 11.

**Adjustment if you transferred liability.** If you transferred the liability for the employer's share of social security tax to the employer (client), you must reduce the amount reported on line 11 by the amount of social security tax included on Form 941, line 8. Don't just subtract the amount reported on Form 941, line 8, because that line includes both social security tax and Medicare tax.

Line 11 (before considering Form 941, line 8)  
– Amount of social security tax included on Form 941, line 8  
= Final Amount to enter on line 11

**Example.** You entered \$12,400 on line 8 and zero on line 9. Line 10 was also \$12,400. 50% of line 10 is \$6,200. However, this amount must be adjusted because you reported \$6,120 (\$4,960 of social security tax and \$1,160 of Medicare tax) on Form 941, line 8. You must subtract \$4,960 (amount of social security tax reported on Form 941, line 8) from \$6,200 (50% of the amount reported on line 10) and enter \$1,240 on line 11.

**Adjustment if you didn't transfer liability.** If you didn't transfer the liability for the employer's share of social security tax to the employer (client) and you paid the employer social security tax on the third-party sick pay that you paid on behalf of the client, you must reduce the amount reported on line 11 by any employer social security tax (included on line 5a) that was for the employees of the client.

Line 11  
– Amount of employer's share of social security tax included on Form 941, line 5a, column 2  
= Final Amount to enter on line 11

**Example.** You entered \$12,400 on line 8 and zero on line 9. Line 10 was also \$12,400. 50% of line 10 is \$6,200. However, this amount must be adjusted because the amount from Form 941, line 5a, column 2, that was entered on line 8 included the employer's share of social security tax that you paid for the wages paid to your client's employees. There isn't a line on Form 941 that can assist in this calculation but you still must determine the amount of Form 941, line 5a, column 2, that was for wages paid to your client's employees. For purposes of this example, if you determine that \$5,000 of employer's social security tax included on Form 941, line 5a, column 2, was attributable to your client's employees, you must subtract \$5,000 from \$6,200 (50% of the amount reported on line 10) and enter \$1,200 on line 11.

### Section 3121(q) Notice and Demand

If you received a Section 3121(q) Notice and Demand (Letter 3263 or Letter 4520) during the quarter, you report the amount for the employer's share of social security tax and Medicare tax on Form 941, line 5f. Letter 3263 or Letter 4520 includes an attachment that shows the employer's share of social security tax. You must add the employer's share of social security tax to the amount reported on line 11.

Line 11 (before considering a Section 3121(q) Notice and Demand)  
+ Employer's share of social security tax from Letter 3263 or Letter 4520  
= Final Amount to enter on line 11

**Example.** You entered \$6,200 on line 8 and \$12,400 on line 9. Line 10 was \$18,600. 50% of line 10 is \$9,300, but you also reported an amount on Form 941, line 5f, because you received Letter 3263. Letter 3263 showed unreported tips of \$20,000 and tax due of \$1,530. The attachment to Letter 3263 listed your liability for tax on unreported tips as follows.

- Employer' share of social security tax: \$1,240
  - Employer's share of Medicare tax: \$290
- You must add \$1,240 (employer's share of social security tax from Letter 3263) to \$9,300 (50% of the amount reported on line 10) and enter \$10,540 on line 11.

## Line 12

Enter the smaller of line 7 or line 11. Also enter this amount on Form 941, line 11. If line 12 is less than line 7, the remaining amount can be used on a Form 8974 for the next quarter.

**Paperwork Reduction Act Notice.** We ask for the information on Form 8974 to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You're not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its

instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Code section 6103.

The time needed to complete and file Form 8974 will vary depending on individual circumstances. The estimated average time is:

|  |         |
|--|---------|
| <b>Recordkeeping</b> . . . . .                             | 45 min. |
| <b>Learning about the law or the form</b> . . . . .        | 1 hr.   |
| <b>Preparing and sending the form to the IRS</b> . . . . . | 1 hr.   |

If you have comments concerning the accuracy of these time estimates or suggestions for making Form 8974 simpler, we would be happy to hear from you. You can send us comments from [IRS.gov/formcomment](https://www.irs.gov/formcomment). Or you can write to the Internal Revenue Service, Tax Forms and Publications Division, 1111 Constitution Ave. NW, IR-6526, Washington, DC 20224. Don't send Form 8974 to this address. Instead, see *Where Should You File?* in the Instructions for Form 941.

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