



# RESEARCH & DEVELOPMENT TAX CREDITS FOR ASSOCIATED BUILDERS & CONTRACTORS

# TAX POINT ADVISORS

...is a National Tax Consulting Firm.

...has 30 years of collective R&D tax incentive expertise.

...works closely with CPA firms nationwide.

...staff includes professionals with fabrication, engineering and manufacturing backgrounds.

...clients include steel fabricators, electrical contractors, engineering services, civil and architectural engineering firms and a wide variety of construction industry businesses.

...offers strategic audit defense options.

# R&D TAX CREDIT IN CONTEXT

- Credit is economic stimulus to keep innovation and creativity on USA soil and spur job creation
- Originally legislated by Congress in 1981 and extended 15 times
- 39 states have adopted state R&D incentive-based programs
- Multiple countries have adopted R&D incentive programs based on the U.S. program
- China now ranks second in the world behind USA in R&D spending

# RECENT LEGISLATIVE CHANGES TO R&D CREDITS

## **QUALIFICATION:**

Relaxation of “Discovery” Test: Evolution of discovery of information from  
‘new to the world’ to ‘new to me and my company or my company’s client’

## **QUANTIFICATION:**

Creation of Alternative Simplified Credit (ASC)

- Incremental creditable amount not tied to company gross receipts
- Limited to timely filed returns (including extensions)

## **UTILIZATION:**

(Sept 2010) Federal R&D tax credits can now offset AMT (YE 2010)

(Dec 2010) Federal R&D tax credits extended thru 2011

# LEGISLATIVE CHANGES TO R&D– THE RESULTS



- 14,000-16,000 U.S. companies claim federal R&D credits annually
- Roughly \$8 billion credits claimed per year
- Approximately 70% of credit dollars are used to pay salaries of workers conducting R&D, encouraging more high-paying U.S. jobs
- 25% of companies claiming credit have assets under \$1m

# LEGISLATIVE CHANGES TO R&D– THE RESULTS

R&D Tax Credit Activity NOT limited to “Basic Research”  
(i.e. laboratories & scientists)

- Available to “Applied Research” (i.e. activity on the shop floor)
- Available to those using engineering or science to solve a customer’s specific problem or need
- Available to those combining existing technologies in new or improved fashion
- Available to those building cheaper, faster or ‘greener’

# QUALIFIED R&D ACTIVITY

## THE FOUR-PART TEST

1. The Activity is Intended to Develop a New or Improved Business Component (Product or Process)  
Create a...Product, Process, Technique, Formula, Invention, or Final Design  
To Improve...Performance, Functionality, Reliability, or Cost
2. The Activity is Technical in Nature
3. The Activity Seeks to Eliminate Technical Uncertainty
4. The Activity Follows a Process of Experimentation

# A LOOK AT QUALIFYING ACTIVITY

Does the R&D Activity done on the Business Component establish or enhance...

( Business Component)	Function	Performance	Reliability	Quality	Durability
<b>Product</b>	✓	✓	✓	✓	✓
<b>Process</b>	✓	✓	✓	✓	✓
<b>Computer Software</b>	✓	✓	✓	✓	✓
<b>Technique</b>	✓	✓	✓	✓	✓
<b>Formula</b>	✓	✓	✓	✓	✓
<b>Invention</b>	✓	✓	✓	✓	✓

# QUALIFIED R&D EXPENDITURES

1. In-House R&D Wages
  - Wages for Direct Labor (Box 1 W-2)
  - Management/Officer & Supervisory Allocation
2. Supplies
  - Costs to fabricate prototypes or items consumed in R&D
3. Contract R&D Wages
  - Outside Labor : 1099 & Vendors (NOT Funded)
4. Exclusions:
  - Funded
  - Non-U.S.

# TYPICAL QUALIFYING INDUSTRIES IN CONSTRUCTION FIELDS



Steel Fabrication

Electrical Engineering

Civil Engineering

Architectural Engineering

Job Shops of all kinds (HVAC, metal fabrication, etc.)

Subcontracting to General Contractors

Green Design and Technology

# QUALIFYING ACTIVITIES IN CONSTRUCTION INDUSTRIES

Construction contractors are often unaware that they may qualify for R&D tax credits. Construction projects sometimes do qualify and sometimes do not.



Here are typical examples of both qualifying construction work and work not qualifying for R&D tax credits:

# NON-QUALIFYING ACTIVITY

Example: A contractor is required to build a structure on a landfill. The contractor performs soil studies to determine ground composition and the land is surveyed. The test results show the ground is unstable and is settling. As a result, the contractor adjusts the footing designs according to the known testing results.

This does not constitute qualified research because the soil testing and surveying employ existing, readily available knowledge and technology. The use of this information to adjust the footing design also employs standard calculations. Accordingly, this project does not qualify for the credit because it fails to meet the two aforementioned tests (New Process or Eliminate Technical Uncertainty).

Routine construction design can incorporate long established load distribution calculations and environmental condition measuring tools to establish one design; this typically won't count as R&D.

# QUALIFYING ACTIVITY

Example: A contractor is required to build a structure in swampy soil. This type of structure has not been built on this type of soil before, so soil testing is performed to determine its friction coefficient. This information is used to design caisson configurations to account for the change in axial loads. In addition, the low friction coefficient of the soil is used to determine materials that must be used for the footing of the structure. The information is not readily available because this structure has not been built on this type of soil before.

These design activities constitute qualified research because the unknown components of the environmental variables resulted in several design alternatives that required theoretical and physical evaluation. Also, the resulting design will become a construction standard for the contractor in similar situations, which satisfies the permitted purpose test.

Note that qualified research and experimentation generally occurs for a construction contractor when construction “standards” are being established. These construction standards may focus on improving safety, structural integrity, symbiotic relationships with seemingly unrelated components, or construction efficiency.

# BENEFIT TO THE COMPANY

- Credit Study can cover all open tax years (go back 3-4 years or more)
- Credit can reduce tax liability dollar for dollar subject to Alternate Minimum Tax (AMT)
- Credit in excess of tax liability or AMT can carry forward for up to 20 years
- Project costs deductible in year of project / payment
- In addition to federal credits, 39 states have R&D Tax Credit programs, some with richer credits than the federal program
  - Some states have credit rates in excess of the federal
  - Some states have credits that are refundable in excess of tax liability

# MANAGEABLE ISSUES

- The client did not have R&D credits in mind when undertook the activity
- Client has little or no documentation
- Qualified Research Activities (QRAs) resulted in failure
- Credit Study will take too long (not a good cost/benefit)
- Cannot currently use credit (NOLs, etc): carry-forward 20yrs
- Audit Concerns: Tax Point Advisors has 100% success rate to-date; never had credit denied under audit

# QUESTIONS / NEXT STEPS

Are you in a qualifying industry?

Have you paid taxes in the past 4 years (tax liability)?

Do you expect to have tax liability this year or coming years?

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