

Research and Development Tax Incentives



Siouxland Chapter CFMA
September 14, 2016



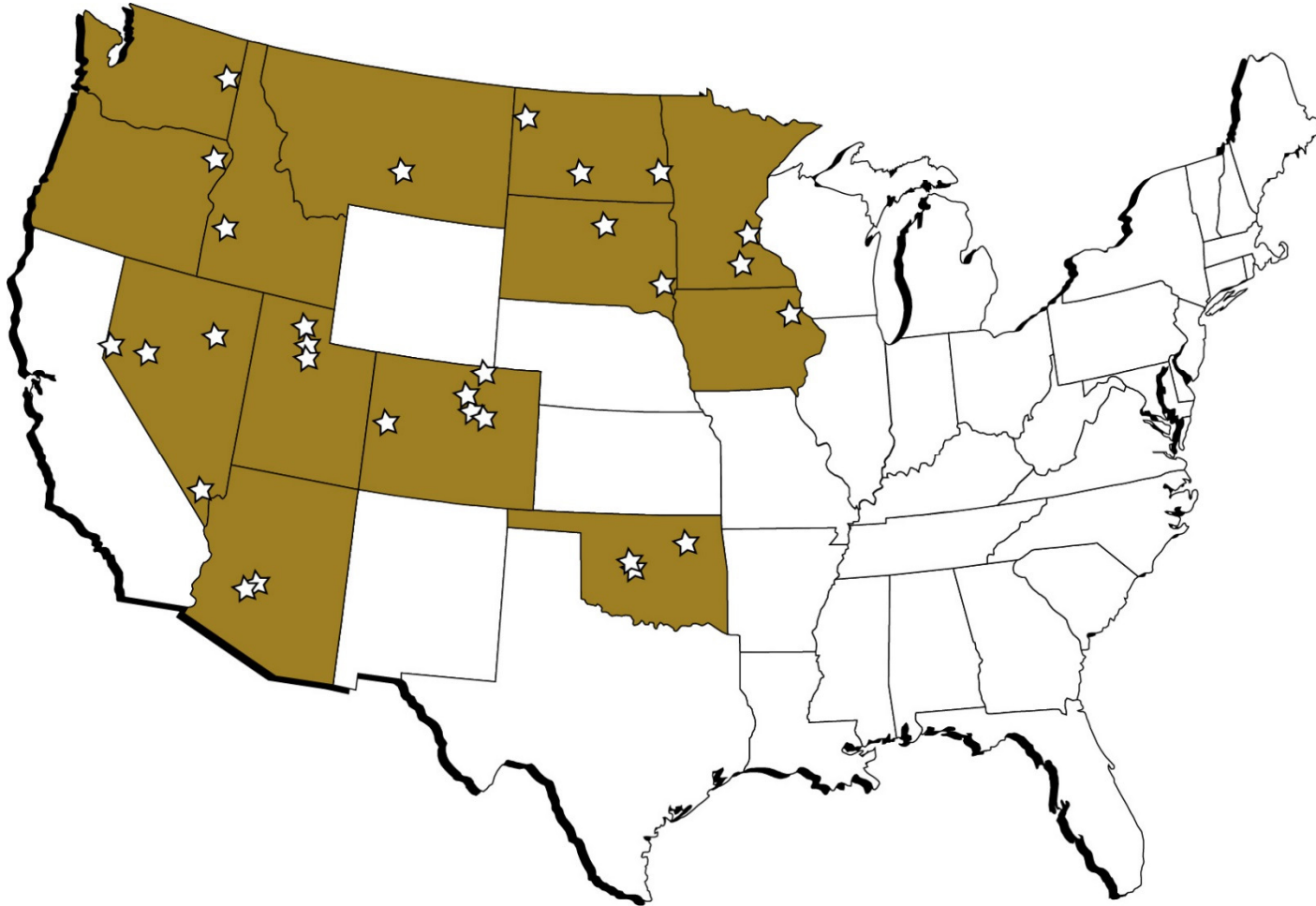
CPAs & BUSINESS ADVISORS



About Eide Bailly

- Top 25 Accounting Firm
- 1,600 Professionals
- Serving 54,000 Clients
- 29 Offices in 13 States

Eide Bailly Locations





Eide Bailly – Focus on Construction Industry

- More than 90 years of experience serving the construction and real estate (CRE) industry
- Currently serve more than 1200 CRE clients across a variety of sectors
- Services we provide to our CRE clients:
 - Audit & Assurance
 - Tax Compliance & Consulting
 - Research & Development Tax Incentives
 - State & Local Tax Consulting
 - Cost Segregation Studies
 - International Tax Consulting
 - Technology Consulting

R&D Incentives - Objectives

- Introduction to R&D tax incentives
- How to qualify for the credit
- Calculation of the credit
- Recent developments / credit enhancements
- Documentation considerations



R&D Incentives - Introduction

- Why have tax incentives for research & development?
 - Promote innovation
 - Help US companies remain competitive
 - Entice companies to remain in the US and / or a given state



R&D Incentives – Introduction

- Types of R&D tax incentives in the US
 - Deduction / amortization of R&D costs
 - Federal R&D credit
 - State incentives



R&D Incentives – Introduction

- R&D Tax Credit benefits
 - Maximum net Federal R&D credit is typically 5% - 7% of eligible expenses
 - Permanent tax benefit / cash savings
 - Can evaluate for all open years (typically current year and 3 prior years)



R&D Incentives – Introduction

- Broad definition of R&D
- Incremental credit – requires computation of a base amount to claim the credit
- Non-refundable credit
 - Credits earned through 2015 only offset regular tax
 - New legislation allows certain companies to offset alternative minimum tax (AMT) and/or payroll tax for future years



Qualification Criteria

- New or improved “business components”
 - Products
 - Processes
 - Software
 - Techniques, inventions, etc.



Qualification Criteria

- 4 Part Test
 - Permitted Purpose – new or improved function, performance, reliability, or quality
 - Uncertainty – capability, methodology, appropriateness of design
 - Experimentation – evaluation of one or more alternatives to resolve uncertainty
 - Technological in Nature – relies on the hard sciences



Qualification Criteria

- Types of construction industry activities that typically qualify
 - Constructability analysis
 - Evaluation of different design alternatives
 - Geotechnical solution design
 - Integration of technology into solutions
 - Design of systems / subsystems with new or different functionality
 - Analysis of alternative construction materials
 - Design of remediation solutions
 - Evaluation of new or improved construction techniques
 - Sustainable architecture / "green" concepts
 - Value engineering



Qualified Research Expenses (QREs)

- Wages
 - Direct involvement, direct support, direct supervision
- Supplies
 - Materials / supplies used in the research
- Contract research
 - 65% of eligible costs



Calculation Alternatives

- Regular credit
 - Base amount relies on data as far back as 1984
 - 20% credit of costs over base amount
 - Maximum net benefit 6.5% of QREs
- Alternative simplified credit (ASC)
 - Base amount relies on 3 prior years' data
 - 14% credit of costs over base amount
 - Benefit usually ranges from 5% - 7% of QREs



Profile - Construction companies that may benefit from R&D tax credits

- Contractors that employ technical personnel (e.g. engineers, designers, architects, etc.)
 - or have others filling this type of role (e.g. project managers, superintendents, etc.)
- Profitable (or will be soon) or start-up company
- High percentage of fixed price work
- Different CRE companies that typically qualify
 - Engineering firms
 - Architectural firms
 - General contractors
 - Mechanical contractors
 - Electrical contractors
 - Fabrication contractors (e.g. steel fabricators)

»»» Case Study – Architecture & Engineering

- Architectural firm — specialize in hospitals
- Revenue \$13M
- Most jobs are fixed price contracts
- 1 year study
 - \$2M qualified expenses (all wages)
 - Combined \$235K of federal / state credits



Case Study – General Contractor

- Wide array of commercial, government, industrial projects
- Revenue \$50M
- Several large Design-Build projects each year; many projects are fixed price
- Work in preconstruction phase includes preliminary design, constructability issues, etc.
- 3 year study
 - \$500K - \$1M qualified expenses each year
 - Combined \$130K of federal credits



Case Study – Mechanical Contractor

- Mechanical systems for various office, municipality, and medical facilities
- Revenue \$20M
- Work involved assessing constructability issues, value engineering, mechanical design services
- 1 year study
 - \$600K qualified expenses
 - Combined \$60K of federal / state credits



Recent Development – Credit Enhancement

- Federal R&D credit made permanent in December 2015
- Businesses with less than \$50M in gross receipts
 - Use R&D tax credit to offset AMT beginning in 2016
- Businesses with gross receipts starting in 2012 or later, and less than \$5 million in gross receipts
 - Use R&D tax credit to offset payroll taxes beginning with 2016 credits (to offset payroll taxes in 2017)



Documentation

- No specific record keeping requirement
- Internal revenue service is often aggressive
 - Key IRS focus in on documentation / substantiation
- Taxpayers should gather / retain contemporaneous records proving the following:
 - Activities meet the 4 part definition of qualified research
 - Expenses incurred meet the statutory requirements
 - Nexus between qualified activities and qualified costs



Questions?

Joe Stoddard

jjstoddard@eidebailly.com

801-456-5915