

R&D Tax Credit Basics

The R&D tax credit is available to any business investing in new or improved products or processes. Manufacturing, Computer software, Technology and Engineering companies can typically qualify for some level of credit. The Federal rules are discussed below, but numerous states have R&D credits as well.

Generally, there are two ways to calculate the credit; the “Fixed Base Percentage” and “Alternative Simplified Credit” methods. The maximum credit amount is approximately 6.5% of the Qualified Research Expenses or QREs. QREs consist of wages, supplies and contract development.

To qualify, expenses need to be related to Qualified Research Activities or QRAs. The taxpayer has to be at risk (have legal rights to the results and economic risk) for the activities to qualify and they must meet the Four-Part Test as follows:

1 Permitted Purpose

Intended to develop or improve a product or processes

- Functionality/Performance
- Quality/Reliability
- Cost Reduction
- Not Aesthetics

2 Technical Uncertainty

Determined at the beginning of a project

- Capability or Methodology uncertainty for developing or improving a product or process
- Design uncertainty
- CAN we reach our goal? HOW are we going to reach our goal?

3 Process of Experimentation

Evaluation of Alternatives

- Prototyping/Testing/Modeling
- Simulation

4 Technological in Nature

Activity must rely on principles of one of the hard sciences

- Engineering
- Physical Sciences
- Computer Sciences
- Biological Sciences
- Not soft science, ie Marketing, Social, Economic or Psychological Sciences

Potential QRAs

Engineering & Designing New or Improved Products or Processes, Prototypes, Materials Testing, Tooling Design, Software Development, Drug Research, Quality Assurance, FEA, and Modeling.

Potential Industries

Any Manufacturing with Engineering Activity such as Plastics, Metal Stamping & Forging, Tool Builders, Machine & Equipment Builders, Chemicals and Electronics. Firms involved with Software Development, Life Sciences and Food Sciences.

For more information on R&D Tax Credit Basics, or how MRPR can assist you, please contact:

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