

## Is Your Company Leaving Powerful Tax Credits on the Table?

By Rizwan Virani and Justin DiLauro, J.D, [alliantgroup](#), LP

In the era of big government bailouts, many small and mid-sized manufacturers, engineering design firms, and other businesses are wondering, "Where is our bailout?" and "Where is our tax relief?" Many of these business owners do not know that as part of the Economic Stimulus Act of 2008, Congress extended existing tax incentives and introduced new ones for all businesses. For example, one of the more popular tax incentives, the research and experimentation (R&D) tax credit has been extended again and has a chance to become permanent. Both chambers of Congress are currently considering legislation that would make the tax credit permanent and increase the Alternative Simplified Credit from 14 percent to 20 percent. The R&D credit, which defines R&D for tax purposes with much broader language than the traditional sense of the term, has provided billions of dollars in tax relief to small and mid-sized businesses for decades. Companies engaging in developing new or improved products or manufacturing processes, or even software for their trade or business, can take advantage of this lucrative tax credit.

As engineers who have worked with many manufacturers in the semiconductor, aerospace, metal fabrication, and other industries, it is apparent to us that many companies have misconceptions about the R&D tax credit. For example, the new or improved products or processes developed at a company do not have to revolutionize their industry or lead to an invention that can be patented. Section 41 of the Internal Revenue Code (the applicable tax laws and regulations), in fact, simply requires that a product or process be new or an improvement for the individual taxpayer.

Many of the country's leading technology companies already take advantage of the research and development tax credit each year. Yet many of these companies inadvertently leave hundreds of thousands of dollars in tax credits on the table because of improper tax credit analysis or substantiation. What follows are two examples of clients who were able to obtain substantial savings for their businesses.

### **Electronics Co., Inc.: "Only engineers qualify, right?"... Wrong!**

This particular national designer and manufacturer of electronic components and assemblies filed for the R&D tax credit every year since the credit was enacted in 1981. Through the years, the tax credit had been a valuable resource for offsetting a small portion of the costs incurred while designing and developing better and more advanced products to remain competitive in the global marketplace. Though this company was capturing costs for certain engineers, they failed to identify all of the qualified research expenditures for each stage of the development process. An accurate analysis and assessment of every development phase from concept design to pre-production identified significant additional expenditures related to employee involvement in R&D and supplies consumed during testing and prototyping, which were then captured for the credit. The additional activities included development meetings, prototyping, testing, and evaluation activities; not just engineering design time.

Upon reviewing the company's qualified research and development undertakings, we were able to help the company identify federal and state tax savings in excess of \$3,000,000. The recouped savings allowed the company to expand its research and development efforts by hiring additional engineers.

### **Aerospace Co., Inc.: "We did not increase our R&D costs this year, do we still qualify?"... Yes!**

Another success story involves a leading manufacturer of aerospace components. Although the company was aware of available R&D tax credits and knew that at least some of its activities qualified, it did not pursue capturing these credits because of their misconception about the credit mechanics. Specifically, the company understood that R&D tax credits are incremental benefits over an applicable base period. However, since the taxpayer and its former accounting firm (a large in-

ternational firm) were not R&D tax credit experts, they were misinformed as to the definition of a qualified research activity – resulting in a false assessment of the company's incremental research over the base period. Therefore, it did not pursue R&D tax credit claims of any significance for many years.

When their new CPA firm introduced them to us, we conducted an in-depth review of the base period and an analysis of available alternative methodologies in calculating these credits, enabling the company to maximize the available qualifying research expenses for the current and previous three taxable years. The analysis resulted in tax savings in excess of \$1,000,000.

While CPA firms may well understand all the relevant tax law and regulations, very few have the in-house technical expertise in engineering and manufacturing to accurately qualify and quantify the R&D tax credit. Conversely, while companies know their own business better than anyone, they generally don't have the tax expertise to know how to successfully claim the credit. Not only are laws and regulations involved, but also case law from tax court and other venues. For these reasons, outside firms, such as [alliantgroup](#), with extensive expertise and experience in both in tax law and the disciplines of manufacturing and engineering, are generally called in either by the engineering firm or their CPA.

With the current economy, it is ever more important for businesses to seek all available tax credits and incentives, and with more than 7,000 federal and state tax credits and incentives available, manufacturing and design companies need to fully understand their eligibility for these incentives — and that sometimes what appears to be too good to be true, really is true.

*Justin DiLauro is an Associate Director at [alliantgroup](#). He holds a B.S. in industrial engineering and a J.D.*

*Rizwan Virani is a proud IEEE member and an Associate at [alliantgroup](#) and holds a B.S. and M.S. in electrical engineering.*