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Research and Development Tax Credits Are Not Just For Big Players

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It is rare that tax issues generate excitement for engineering, design, and construction firms, but significant research and development-related tax benefits can be available to firms engaged in creating energy efficient buildings for the government.

Three key things to consider when working to maximize your firm's project-related tax benefits include the Research and Development tax credit, the 179D deduction, and avoiding the mistake of "self-censoring," or assuming your firm's activities will not qualify.

The R&D tax credit is a government-endorsed incentive that many engineering, design, and construction firms – particularly small and mid-sized ones—fail to claim, either from lack of information or from self-censorship.

If your firm is developing new or improved features or functionality through a documented development process, you should be taking advantage of this credit. At \$9 billion a year, the R&D credit is one of the most generous tax benefits established by Congress.

Engineering, design, and construction firms often create new methods and approaches for projects as they are designed and implemented. Improvements made to the energy efficiency of a building or other structures can qualify for tax incentives. People in lab coats are not the only ones with innovative ideas that solve problems and increase efficiency. Congress designed the R&D tax credit to encourage innovation in every industry.

The 179D Energy Efficient Deduction comes into play when architects or engineers work on qualifying projects for local, state, or federal governments. According to the law, eligible companies that perform energy efficient design work on new, renovated or retrofitted government buildings can garner a deduction of up to \$1.80 per

square foot for projects placed into service from 2006 to 2013. “Garner” is the operative word, though: since government entities do not pay taxes, they can only transfer the deductions to firms that designed or engineered the work.

Firms face two main challenges in securing the 179D deduction: first, they need government entities to assign the 179D tax deduction to them; and, second, they need to have the correct documentation in place to maximize the tax benefits.

The IRS requires that the architect or engineer receive a letter from the government entity assigning the tax deduction to their firm. The letter has all sorts of required bells and whistles, and securing the required signature may not be a walk in the park. Firms may benefit from the services of an advisor specializing in this area, such as our firm. There also is a bit of a race against time since the three-year look-back period is expiring soon, and others involved in the design of the building may seek the same letter and tax benefits for the same project. Delays can be costly.

And to maximize the tax benefits, the law requires extensive testing of innovative solutions. Activities and costs associated with creating those tests should be recorded. A third-party engineer’s independent determination of the building’s energy efficiency also is required to certify the amount of the tax benefits that will be available. We have seen architects and engineers leave money on the table too often by failing to document their applications correctly.

But the biggest risk for small- and medium-sized businesses is self-censorship. Large companies, with armies of tax lawyers, are all over R&D credits, while too many smaller companies act as if the R&D credits do not apply to them.

Smaller companies may not realize that their activities related to the design and development of many types of systems can constitute qualified R&D activities, potentially entitling them to significant R&D incentives.

You don’t have to be a manufacturer or software developer to be conducting qualified activities as defined by the Internal Revenue Code.

Innovation in engineering, design, and construction happens each day on many different scales. The cost of projects can be reduced when R&D tax incentives are claimed for time and materials. Firms of all sizes should pursue tax credits to reduce their tax obligation and improve operating cash flow.

Rizwan Virani is an alliantgroup Managing Director leading the firm’s Architecture & Engineering, and Construction teams, as well as the Energy Efficient Commercial Building Deduction (179D) Team. He has a B.S. in Electrical Engineering and M.S. in Engineering Management from The University of Texas. Rizwan is passionate about educating engineers and has helped several hundred take advantage of tax incentives, helping them continue to grow their practices, hire new employees, and to remain competitive in today’s economy.