

Research and Experimental (R & D) Tax Credits

IRC Section 41

Presented By:

Kevin Corley, CPA
alliantgroup, LP



alliantgroup®

alliantgroup, LP

- **alliantgroup** - Houston (national office), New York, Boston, LA, Atlanta, Orange County, San Francisco, San Diego, Seattle, Chicago, Denver and Miami
- **alliantgroup** - Has over 200 professionals nationwide
 - Former “Big Four Partners” and Managers
 - CPAs and Attorneys
 - Engineers, Software Programmers, Chemists, Biologist, etc
- **alliantgroup** - Only specializes in government sponsored incentive programs.

Executive Summary

- 17,700 firms claimed the credit in 2005
- California reported the most activity with Texas and Massachusetts following
- 1,100 firms took \$5.7 B out of 7.2B (80%)
- Manufacturing took 71.2% of the credit
- Professional Services took 12.4% of the credit
- Historically the realm of the Fortune 1000 Firms

1981-2001

- Identify the QRAs – qualified research activities
 - **Was discovery test (patents, inventions)**
 - **Was extensive documentation**
- Calculate the QREs – qualified research expenditures
 - Wages
 - Supplies
 - Contractors
- Calculate the Credit – Form 6765

Rule Change - New Regulations

- Proposed 2001, Final 2003
 - To keep innovation and creativity in the U.S.
- The proposed and final regulations:
 1. Eliminated the Discovery Requirement
 2. Modified the Documentation Standard
- R&D is no longer only:
 - scientists, lab coats, patents, etc.
- **Clearly Defined:** Congress made it clear through legislative history that the credit should NOT impose unreasonable record-keeping requirements.
- Increase in budget:
 - **\$9B**

2001-2007

- Identify the QRAs – qualified research activities
 - **4 criteria replaced discovery test**
- Calculate the QREs – qualified research expenditures
 - Wages
 - Supplies
 - Contractors
- Calculate the Credit – Form 6765

“Traditional” Versus “Tax”

Traditional Definition



Tax Definition

“Four Main Requirements”

1. New or Improved Business Component
2. Technological in Nature
3. Elimination of Uncertainty
4. Process of Experimentation

1- New/Improved Business Component

Business Component Purpose Matrix					
	The Purposes of the R&D Activities Related to the:				
	Function	Performance	Reliability	Quality	Durability
Product	✓	✓	✓	✓	✓
Process	✓	✓	✓	✓	✓
Computer Software	✓	✓	✓	✓	✓
Technique	✓	✓	✓	✓	✓
Formula	✓	✓	✓	✓	✓
Invention	✓	✓	✓	✓	✓

2 -Technological in Nature

➤ **Includes - Hard Sciences:** Research must rely on principals of hard sciences

- Physics
- Chemistry
- Biology
- Computer sciences

➤ **Excludes - Soft Sciences:** Research can not be in the soft sciences

- Economics
- Psychology
- Management sciences, etc.

3 - Elimination of Uncertainty

➤ **R&D Activities Must Be Intended to:**

- Discover information
- Eliminate uncertainty concerning the companies capability, process or final design.

➤ **Exists if Taxpayer is Uncertain:**

- Can We? – Can company develop the business component?
- How? – How can company develop the business component?
- Final Design ? – What will the final business component look like?

4 - Process of Experimentation

➤ **Development Activities:**

- Must evaluate a process and its alternative
- Must be designed to achieve a result that was uncertain at the outset

➤ **May Involve:**

- One or more hypothesis
- Testing and analyzing the hypothesis
- Refining or discarding the hypothesis as part of a design process

➤ **Must Engage in Process of evaluating & testing alternatives through:**

- Modeling
- Simulation
- Systematic trial and error

➤ **Failure:** The taxpayer does not need to “succeed”

Skills Used

- Chemists
- Engineers
- Biologists
- Programmers
- Technical Writers – to document activities, defend in case of audit/interpret code
- CPA/Trusted Advisor
- Computer Scientists
- Attorneys
- Tax Attorneys

What Makes this Credit so Powerful?

1. New Regulations Finalized December 2003

- Easier for a broader array of companies to qualify their activities as R&D
- They provide greater flexibility in satisfying certain record keeping requirements

2. Apply new regulations for all **open tax years** – (i.e. 2005, 2006, and 2007) = Significant Cash Refunds Plus Interest

3. Middle-Market Companies **typically conduct more R&D as a percentage** of revenue (i.e., CEO on down.... Marketing / Production / Administration / Purchasing / Information Technology, Quality Assurance / Engineering / Other)

4. Conservative / Government Sponsored Incentive

Results – R&D!

Industry	Revenue	Tax Credits
Apparel - Women's High End Fashion	\$21 MM	\$804,000
Custom Bedroom Furniture	\$8 MM	\$100,000
Cabinet Manufacturer	\$63 MM	\$362,000
Nutritional Supplements	\$18 MM	\$218,000
Napa Winery	\$6 MM	\$220,000
Offshore Marine Construction Co.	\$250 MM	\$3,400,000
Software Development Co.	\$7 MM	\$800,000
Injection Molding Co.	\$100 MM	\$5,500,000
Job Shop / Manufacturing Co.	\$15 MM	\$400,000

Form 6765 (2007)

- Regular Credit
 - 20% Eligible Expenses
 - 13% Eligible Expenses (280c)
- Alternative Incremental Credit
 - 3% – 5% over base
- Alternative Simplified Credit
 - 12% over prior 3 year average QREs (6% if no prior year QREs)

Eligible Costs

- Wages
- Supplies
- 65% of Qualified Contract Research
- Cannot Take Depreciable Assets

ABC Range Corporation

Snapshot of 2007 Results

Total Qualified Wages	\$4,352,755 (approx 12% of total wages)
Total Qualified Supply Costs	\$188,145
Total Qualified Contractor Expenses	\$1,463,858
Net Federal Benefit (Alternative Simplified Credit)	\$344,044

ABC Range Corporation

Summary of Activities



Commercial Cooking Products

Project Cluster – alliantgroup's team identified and documented ABC's process for developing and bringing to market, as well as the new and improved products which were (successfully or unsuccessfully) developed through this process



Refrigeration Projects – alliantgroup's team identified and documented fourteen (14) new development projects undertaken by ABC's Refrigeration in 2007, including the design of a new generation of controllers for refrigeration units, a new gasket design for all refrigerators, and the design of two new refrigerator models.

ABC Range Corporation

Summary of Activities, cont'd

Kitchen Clean-up Division – 450 Series Dishwasher – In 2007, all activities conducted by the Kitchen Clean-up division were directed towards the design and development of the new ABC 450 Series Dishwasher. Working with ABC's 8-man Kitchen Clean-Up development team, alliantgroup Project Managers identified and documented the primary development process utilized to create the 450 Series, reviewed the results of prototype tests, sourced and documented the qualifying labor expenditures, and drafted technical reports to document and summarize the information.





**Advanced
Composite
Materials, LLC**

1448 S. Bluebonnet Road, Greer, South Carolina, 29615
854-677-0123 Fax: 864-676-6515 www.acm-llc.com

February 16, 2008

**Mr. Kevin Corley
Alliantgroup, LP
Three Riverway
Suite 1400
Houston, TX 77056**

Dear Kevin:

Alliantgroup, LP did an excellent job in getting Advanced Composite Materials, LLC some very sizable R&D tax credits. We were pleased with your work, and the value you provided to our company.

The staff at Alliantgroup was knowledgeable and competent. They were well organized and made the process quite easy. When we went into this agreement, we thought that R&D tax credits were a lot of pain for little value. We were pleasantly surprised. The value brought to Advanced Composite Materials, LLC was immense, and the process was direct and straightforward.

The big question people ask: would we use Alliantgroup again? The answer is an unequivocal yes. We would also recommend Alliantgroup to other companies who have had a growing R&D presence and can benefit from R&D tax credits.

Again, we wish to thank you for a job well done and the excellent value you offer, and we wish you all the best in the future.

Sincerely,

Thomas E. Quanttrill, Ph.D.
President & CEO



Flanders Filters, Inc.
531 Flanders Filter Road
Washington, NC 27889
(252) 946-8081 - Telephone
(252) 946-4738 - Telefax

May 12, 2008

Alliantgroup, L.P.
5400 Westheimer Court,
Suite 700
Houston, Texas 77056

To whom it may concern,

I would like to thank Justin Goodson and the team at Alliantgroup, L.P. for their outstanding work on the R&D Tax Credit study you prepared on behalf of Flanders Filters/CSC/GCS for tax years 2002-2005.

Initially, we were skeptical to engage in this study as we were concerned about the disruption it would cause to our staff, but Mr. Goodson and his team conducted the study with the highest level of professionalism while being respectful of our employee's time.

His knowledge of the process resulted in a final report that was thorough and concise. It was apparent to me that Alliantgroup approaches their business very seriously and with a deep commitment to serving their clients through their due diligence in addressing the rigorous documentation that is necessary to a study that is so complex in nature.

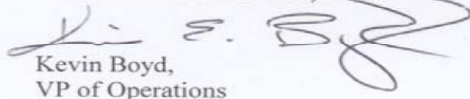
Justin Goodson and Neil Sheth performed two on-site visits wherein they took the time to tour our facility, explaining the intricacies of the R&D Tax Credit and how they applied to the quality filter, clean-room and containment filtration systems industry. He conducted in-depth technical interviews and performed his due diligence in ascertaining the percentage of our wage allocations.

Flanders Filters plans to use these refunds to enhance our operating capital as we view these tax credits as a critical source of funding for the continued growth of our company.

Again, I would like to express my heartfelt appreciation to Justin and the team at Alliantgroup, L.P. for exceeding my expectations. I would highly recommend their professional services to every company that could benefit from the reinvestment of tax refunds they are entitled to as the result of their R&D activities.

Sincerely,

FLANDERS FILTERS, INC.


Kevin Boyd,
VP of Operations



April 16, 2008

Kevin Corley
AlliantGroup
5400 Westheimer Court, Suite 700
Houston, TX 77056

Dear Kevin,

I wanted to take some time to express my appreciation for a job well done on my Research and Development Credit study and on my Sales and Use tax study. Your company has done the R&D study two years in a row, at the completion of which I received a refund in excess of \$300,000.

I found your firm's weekly status updates to be a great way for me to keep in touch with the progress of the study. All of your staff has been very helpful and pleasant to deal with. I particularly want to recommend Matt Hester and Daniel Lewicki. They really know their stuff. I wish that you guys had more of these types of ideas

I would not hesitate to recommend you and look forward to working with you for years to come.

Sincerely,

Derek Hennecke,
CEO and President
Xcelience



COMMERCIAL REFRIGERATOR DOOR COMPANY

6200 Porter Road • Sarasota, Florida 34240
800 217-3840 • 941 571-8110 • Fax 941 377-3850

April 3, 2008

alliantgroup, LP
5400 Westheimer Court, Suite 700
Houston, TX 77056

Re: Letter of Recommendation

To Whom It May Concern:

Jan Kimmel performed the 2003 - 2005 R&D Study as well as the 2006 and 2007 Follow-Up R&D Studies for our company. He exerted the effort to understand our business and its complexities and was very schedule-minded during the course of the project while organizing and conducting our discussions with high sensitivity to our business commitments. Additionally, his ability to communicate the specific details of the R&D Credit and how it applied to our company exceeded expectations.

On the whole, alliantgroup's staff was very polite and responsive to our needs. The work product was comprehensive and thorough, and reflected a high level of diligence, year after year. We were impressed with each Study we received and found alliantgroup to be highly professional and knowledgeable. Our experience with your firm has been very encouraging, and I would highly recommend alliantgroup to anyone who could benefit from your services.

Sincerely,

Tony Gamelin, CPA
Chief Financial Officer

Oscar de la Renta

January 14, 2008

alliantgroup, LP
5400 Westheimer Court, Suite 700
Houston, TX 77056

Re: Recommendation Letter

To Whom It May Concern:

A few years ago I was introduced to the people at the alliantgroup to discuss an R&D tax credit study that ultimately was of significant benefit to Oscar de la Renta, Ltd.

Thanks to a very informative and impressive presentation, on point with the attributes of our business as well. I was able to get a thorough and complete understanding of how the tax code applied to our activity.

Furthermore, alliantgroup work product was excellent and well documented and their ability to deliver a first class product which achieved projected results was very impressive. We found alliantgroup to be very professional, responsive and knowledgeable.

Our experience with the alliantgroup has been very positive, and I would recommend them to anyone who may benefit from their services.

Yours truly,



Giuseppe Celio
Chief Operating Officer
Oscar de la Renta, Ltd.

When good things are rising



February 26, 2008

Kevin Corley
Alliant Group
Three Riverway, Suite 1400
Houston, TX 77056

Dear Kevin,

I want to express my appreciation for the work your firm has done the past six (6) years in conducting our Research and Development Tax Credit Study. Your firm has documented tax credits of \$750,000 over this six (6) year period.

Your staff's ability to effectively ask the proper questions and get the required information without tying up huge amounts of my time or my staff's time was impressive. We felt your company an in depth knowledge of the Internal Revenue Code and has a firm grasp of backup information that is needed in case of an I.R.S. audit.

Please feel free to use my name as a reference as I would recommend your firm very highly. We look forward to using your firm to conduct our 2007 Tax Credit Study.

Sincerely,

A handwritten signature in cursive script that reads "Michael L. Knott".

Michael L. Knott
Vice President Finance



Trek Eight, LLC
100 San Marcos Boulevard
Suite 370
San Marcos, CA 92069
760.750.1978
760.750.1965 Fax

August 29, 2007

Mr. Jim Foster
alliantgroup, LP
Three Riverway, Suite 1400
Houston, Texas 77056

Dear Jim,

I wanted to take just a moment to commend you and your team on the positive experience we have had with alliantgroup, LP. Being a very small technology firm, we were wholly unaware that we qualified for the R&D tax credits until our accountant suggested that we contact your firm to review our payroll and development costs.

For a small, privately funded company, every little bit helps, and we were both surprised at how much we were giving away unnecessarily, as well as pleased that alliantgroup worked with us to develop the tax credits we were ultimately owed.

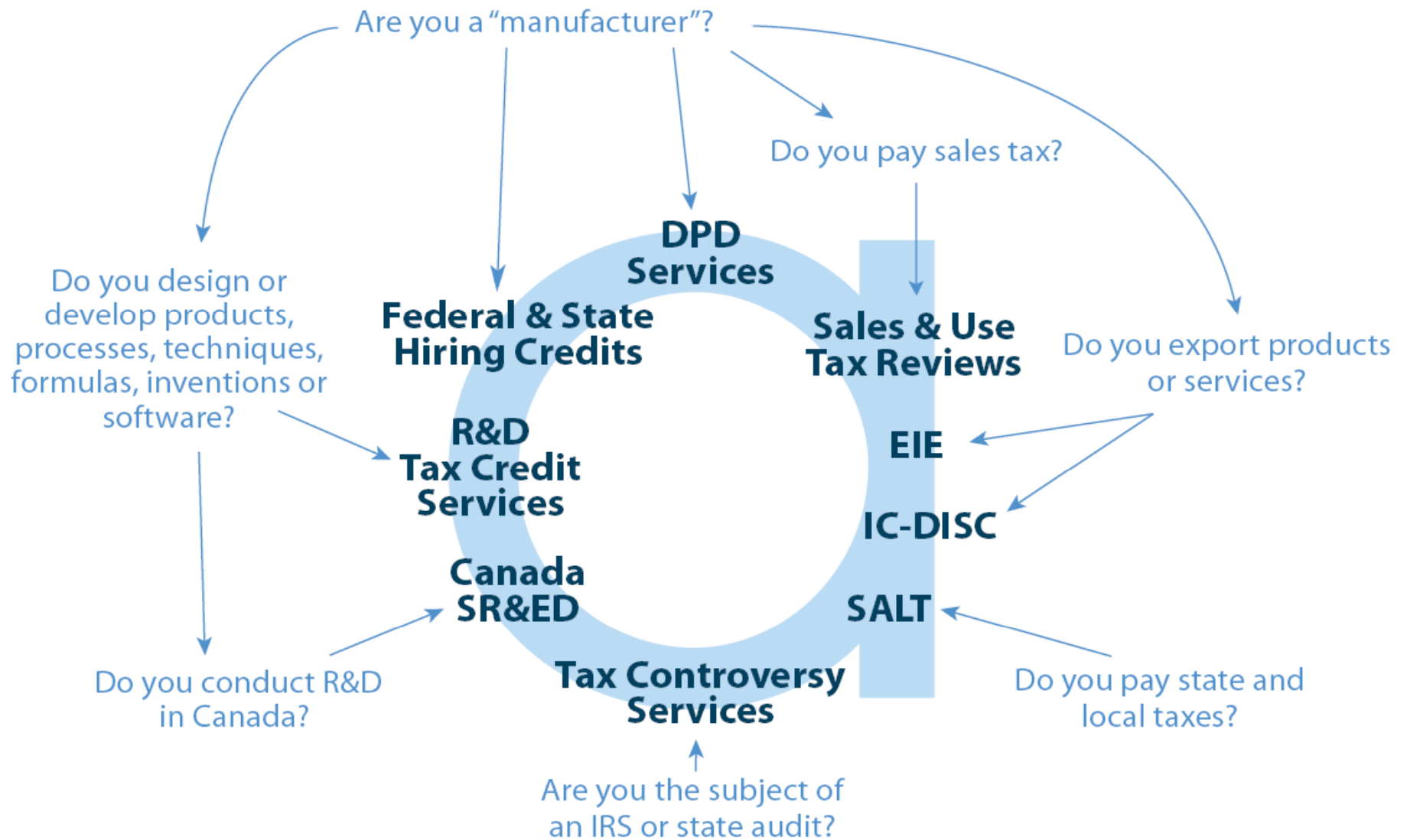
The team at alliantgroup was both proactive and patient, and walked us through each part of the process in a clear and concise manner, resulting in a final report that our accountant was able to use to file for significant tax credits. I absolutely would not hesitate to recommend you, your team, or the alliantgroup to any firm that desires your services.

Sincerely,

A handwritten signature in blue ink, appearing to read "Jamie A. Leasure".

Jamie A. Leasure
President
TrekEight LLC

How can alliantgroup® serve you?



Contact Information

Kevin W. Corley, CPA

(713)376-1958 (Cell)

Kevin.Corley@alliantgroup.com

The logo for Alliant Group is located in the bottom right corner of the slide. It features the text "alliantgroup" in a lowercase, sans-serif font, with a registered trademark symbol (®) to the upper right of the word "group". The text is white and is set against a dark blue background that includes a stylized, glowing blue grid pattern. A light blue diagonal line runs across the background from the bottom left towards the top right, partially overlapping the logo area.

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