

## Taking Advantage of R&D Tax Credits During an Economic Downturn

By: *Randy Crabtree, CPA*

During lean economic times manufacturing and other technology-oriented businesses may find themselves with underutilized employees and spare capacity due to falling order volumes and production decreases.

This may be the optimal time for businesses to think about putting these assets to work by starting new development or improvement projects so that the business can emerge stronger and better positioned when the economy does start growing again. And both the Federal and Arizona state governments may help with this through the tax benefits given through Research and Development Tax Credits.

R&D tax credits are frequently misunderstood, and many companies mistakenly believe that they do not qualify. However, any business, in any industry, that engages in “qualified activities” can take advantage of the credit.

Examples of activities that can both strengthen a business and typically qualify for R&D tax credits include designing or developing automation equipment, improving product quality, experimenting with the use of cheaper raw materials or materials that may be easier to process, and increasing production throughput or decreasing labor costs. Basically, this translates into projects that try to do things “better, faster, or cheaper.”

Whether you are considering product development or process improvement initiatives, to qualify for the credit activities must meet all four parts of the following criteria:

1. **Permitted Purpose** | The project must be intended to be useful in the development of a new or improved business component for the taxpayer. A business component may include a product, process, technique, formula, invention, or software.
2. **Technological in Nature** | The project must be undertaken for the purpose of discovering information that is technical in nature. Thus, the activity must rely on the principles of physical sciences such as engineering, biology, or computer science.
3. **Elimination of Uncertainty** | The project must be intended to eliminate uncertainty related to the development or improvement of a business component. Uncertainty can relate to the components capability, development method, or optimal design.
4. **Process of Experimentation** | The project must evaluate one or more alternative solutions through the development, refinement, and testing of different options. Further, technical risk must be present, which means that there is a chance the project will not be successful.

One last important note to keep in mind if you are considering taking advantage of the R&D tax credit, or if you already are taking the credit: Recent court cases have reinforced the importance of properly documenting and supporting any credits claimed. At a minimum, companies should be able to provide documentation that shows projects were qualified and be able to link qualified expenses back to those qualified projects.

Randy Crabtree, CPA, is a partner with Tri-Merit, LLC. He has over 20 years of public accounting experience and has focused solely on the R&D Tax Credit for the past 3 years. He can be contacted at [rcrabtree@tri-merit.net](mailto:rcrabtree@tri-merit.net) for more information.

Our firm provides the information for general guidance only, and does not constitute the provision of legal advice, tax advice, accounting services, investment advice, or professional consulting of any kind. The information provided herein should not be used as a substitute for consultation with professional tax, accounting, legal, or other competent advisers. Before making any decision or taking any action, you should consult a professional adviser who has been provided with all pertinent facts relevant to your particular situation. This article is not intended to be used, and cannot be used by any taxpayer, for the purpose of avoiding accuracy-related penalties that may be imposed on the taxpayer. The information is provided "as is," with no assurance or guarantee of completeness, accuracy, or timeliness of the information, and without warranty of any kind, express or implied, including but not limited to warranties of performance, merchantability, and fitness for a particular purpose.