

3 Quick questions for startups on R&D tax credit

How can startups benefit from the R&D tax credit?

Eligible startups and early-stage Qualified Small Businesses (QSBs) can use the R&D tax credit to offset payroll taxes by up to \$250,000 per year for five years, generating immediate cash flow that can be complementary to other funding sources. This significant benefit should not be overlooked, especially during uncertain economic times when shoring up cash flow is critical to future business success.



What do startups need to be eligible for the R&D tax credit?

There are specific eligibility requirements for businesses to qualify for the R&D tax credit. The work performed must relate to a field of technology, science or engineering and be undertaken in order to solve technological uncertainties. The company must also follow a systematic process of experimentation during which it evaluates different alternatives to achieve its technological objective. In general, projects that qualify involve the development of new or improved products, technologies, software, or manufacturing processes.



In order to be treated as a Qualified Small Business and be able to use the R&D tax credit against payroll taxes, startups must meet the following eligibility criteria:

- *Less than \$5 million of revenue in the year the credit is claimed*
- *No revenue for any year prior to the period of five years ending with the credit year*

If those two criteria cannot be met, a startup can use the R&D tax credit against its income tax liability or carry the credit forward for future utilization.

What are some key strategies for maximizing the benefit?

Proper documentation is key to benefiting from the R&D tax credit. Qualifying requires substantiating the claim and determining the expenditures associated with each project. Startups need to keep track of the resources allocated and the process involved in any development and improvement projects. For example, keep a project log where all steps of a software development project are documented.



In general, companies tend to underestimate the amount of effort and the complexity inherent to their development and improvement projects. An experienced R&D tax advisor can help startups navigate the complex requirements and claim the credit to generate an immediate bottom-line benefit.