



## **EXECUTIVE SUMMARY**

**DATE:** Thursday, November 16<sup>th</sup>, 2017

**TIME:** 3:00pm-4:00pm EST

**ATTENDEES:** AT&T, Walmart, Siemens, HCA, Bayer, NCR, Northrop Grumman, Medtronic, Commscope, Superior Essex, Kellogg's, Oracle, Stanley Black & Decker, Hormel, Monsanto, Adtran, Jet Blue, Lockheed Martin, Cohu, Duke Energy, Nilfisk, Intercept, MSCI, Domtar, Blackbaud, AGCO, Mission Pharmacal, Liaison Technology, Schlumberger, Paccar, Caterpillar

**SPEAKERS:** Jason Massie and Peter Green of MASSIE R&D Tax Credits, Alpharetta, GA  
Alex Sadler and Doug Norton of Morgan, Lewis & Bockius, LLP, Washington, D.C.  
Urvi Doshi Sood and Noela Thi, The Lockheed Martin, Bethesda, MD

## **AGENDA:**

### **1. INTRODUCTIONS**

Peter Green and Jason Massie  
*Massie R&D Tax Credits, Alpharetta, GA*

### **2. WASHINGTON UPDATE- SPECIAL REPORT**

Alex Sadler and Doug Norton  
*Morgan, Lewis & Bockius LLP, Washington, D.C.*

### **3. PRACTICAL ISSUES WITH DIRECTIVE**

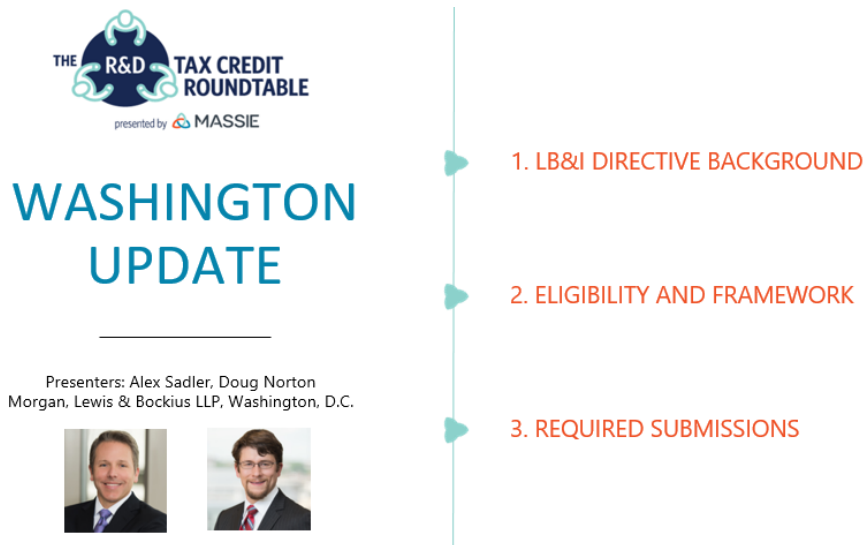
Jason Massie  
*Massie R&D Tax Credits, Alpharetta, GA*

### **4. MEMBER SPOTLIGHT**

Urvi Doshi Sood, Noela Thi  
*Lockheed Martin*

Peter Green opened the Roundtable Meeting and introduced our featured speakers and attendees.

Jason Massie noted that he has been having conferences with large taxpayers about evaluating the LB&I Directive and wanted to focus some time on this Roundtable to discuss further. He invited Alex and Doug to the Roundtable to present their review of the Directive in the Washington Update segment.



Alex and Doug commented that the new Directive appears to be an “administrative solution” which would streamline research credit claims for both taxpayers and the LB&I examiners. The Directive requires taxpayers to keep US GAAP under ASC 730, and reconcile book research expense in detail and in accordance to the format outlined in the Directive and Appendix definitions. There is a reconciliation which must be filled out to tie-down Form 6765 line numbers and amounts to the GAAP amounts.

The required eliminations from adjusted book R&D are outlined in Appendix C and straight-forward. Backing out contract research in this section may cause taxpayers to re-think whether the Directive will negatively impact the overall credit under the Directive since contractor payments will be outside the safe-harbor.

Appendix D outlines the wage details, with new safe-harbor percentages which may be applied to Qualified Individual Contributors and 1<sup>st</sup> Level Supervisors (both at 95%) and Upper Level Managers (at the lesser of actual or 10% of the value of the other two groups). The haircut on the Upper Level Managers at 10% may come into play for organizations with traditional leadership structures, so this computation needs to be modeled to review the overall impact to the credit amounts under 41 versus those under the Directive.

Overall, Alex and Doug thought the directive was “commendable, and a thoughtful step in the right direction” but there were plenty of limitations including: contract R&D costs excluded, wages reduced by 5% can be significant, QREs not under ASC 730 not protected.

Jason Massie was the next presenter for the Roundtable.

# PRACTICAL ISSUES WITH THE DIRECTIVE

Presenter: Jason Massie  
Massie R&D Tax Credits, Alpharetta, GA



- 1. TWO EXAMPLES
- 2. THOUGHTS

Jason went through two practical examples. The first shows how the 10% limitation for Upper Level Supervisors did not hurt the taxpayer given the facts, and even after taking out contractors, when you factor in the cost of losing QREs on audit and time/expense to defend the credit, the net difference between the two methods might make the Directive appealing.

## EXAMPLE 1

- Accounts for R&D using ASC 730
- Has payroll system where QIC, 1<sup>st</sup> LS and ULM can be determined and satisfy the Directive
- All core wages at 100%
- No Sec. 41 credit is attributable to R&D done outside the core departments
- Audit History of sustaining 95% of Wages upon Exam

		W-2, Box 1	S41	S41 QREs	DIR	DIR QREs
WAGES	FTE	Avg Wage				
Individual	2,500	100,000	100%	250,000,000	95%	237,500,000
Supervisor	750	150,000	100%	112,500,000	95%	106,875,000
Upper-Level	100	225,000	100%	22,500,000	100%	22,500,000
<b>Total Wages</b>	<b>3,350</b>			<b>385,000,000</b>		<b>366,875,000</b>
<b>SUPPLIES</b>	<b>25,000,000</b>			<b>25,000,000</b>		<b>25,000,000</b>
<b>CONTRACTORS</b>	<b>25,000,000</b>		65%	<b>16,250,000</b>		<b>0</b>
<b>Total QREs</b>				<b>426,250,000</b>		<b>391,875,000</b>
<b>Total Credit</b>				<b>27,706,250</b>		<b>25,471,875</b>
Under Exam Sustain 95% of Wages Typically				(1,251,250)		0
<b>Adjusted Credit</b>				<b>26,455,000</b>		<b>25,471,875</b>
Less: Provider Fee to do study				?		N/A
Less: Provider Fee to defend study				?		N/A
Less: Internal Time and Effort during study/defend				?		N/A
<b>Net Credit</b>				<b>?</b>		<b>25,471,875</b>

Example two showed how a top-heavy organization, with a sizable number of Upper Level Managers, would be significantly impaired under the Directive.

### EXAMPLE 2

- Accounts for R&D using ASC 730
- Has payroll system where QIC, 1<sup>st</sup> LS and ULM can be determined and satisfy the Directive
- All core wages at 100%
- No Sec. 41 credit is attributable to R&D done outside the core departments
- Audit History of sustaining 95% of Wages upon Exam

		W-2, Box 1	S41	S41 QREs	DIR	DIR QREs
<b>WAGES</b>	<b>FTE</b>	<b>Avg Wage</b>				
Individual	1,350	100,000	100%	135,000,000	95%	128,250,000
Supervisor	1,250	150,000	100%	187,500,000	95%	178,125,000
Upper-Level	750	225,000	100%	168,750,000	10%	30,637,500
<b>Total Wages</b>	<b>3,350</b>			<b>491,250,000</b>		<b>337,012,500</b>
<b>SUPPLIES</b>	<b>25,000,000</b>			<b>25,000,000</b>		<b>25,000,000</b>
<b>CONTRACTORS</b>	<b>25,000,000</b>		65%	<b>16,250,000</b>		<b>0</b>
<b>Total QREs</b>				<b>532,500,000</b>		<b>362,012,500</b>
<b>Total Credit</b>				<b>34,612,500</b>		<b>23,530,813</b>
Under Exam Sustain 95% of Wages Typically				(1,596,563)		0
Adjusted Credit				33,015,938		23,530,813
Less: Provider Fee to do study				?		N/A
Less: Provider Fee to defend study				?		N/A
Less: Internal Time and Effort during study/defend				?		N/A
Net Credit				?		23,530,813

Jason also cautioned taxpayers to review all of the boxes below when making a determination. If you are evaluating the Directive, there are many things to consider.

### THOUGHTS

<p><b>Account under ASC 730</b></p> <p>No  Yes</p> <p> </p>	<p><b>Detailed Books and Records</b></p> <p>No  Yes</p> <p> </p>	<p><b>Loads of Contractors</b></p> <p>Yes  No</p> <p> </p>	<p><b>Lack of Documentation</b></p> <p>No  Yes</p> <p> </p>	<p><b>Lack of Executive Buy-In</b></p> <p>No  Yes</p> <p> </p>
<p><b>Significant Upper Level Manager Wages</b></p> <p>Yes  No</p> <p> </p>	<p><b>Significant State Credits</b></p> <p>Yes  No</p> <p> </p>	<p><b>Poor Exam History</b></p> <p>No  Yes</p> <p> </p>	<p><b>Too many acquisitions and no support</b></p> <p>No  Yes</p> <p> </p>	<p><b>Any after all of these questions?</b></p> <p>Yes  No, then maybe consider the Directive</p> <p> </p>

The last speakers were Urvi Doshi Sood and Noela Thi from Lockheed Martin in Bethesda, MD.



## MEMBER SPOTLIGHT

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**Urvi Doshi Sood**

Vice President, Tax Administration

**Noela Thi**

Lead Sr. Tax Accountant

1. ABOUT LMC AND THE PROCESS

2. BEST PRACTICES/QRE MINING

3. IRS CONTROVERSY EXPERIENCE

Urvi and Noela discussed the challenges in dealing with a company that has over 97k employees worldwide spread out over 400 facilities globally in 70 countries. LMI does have over 50 tax professionals, and has been in CAP since 2008. They annually claim large research credits which have ETR effect of 1.6-2.2% decrease to the rate.

Key takeaways: Collaborative effort between Business Area and Tax Department. Fiscal year to date dollars are pulled from ledgers. Engineering labor is reviewed to narrow qualifying dollars. Questionnaires are sent to program finance people to assist with the annual percentages for wages. The tax department reviews the Business Area workpapers, computes trends, and defends the credits under CAP. They mine for new research areas frequently looking over LMI press releases, the corporate intranet, and other news sources. They also do site visits and engineer interviews periodically to uncover new innovation areas. They carefully review contractor versus supplies expenses, and generally battle the IRS on prototype expenses. Under CAP they provide the IRS data quarterly, and the entire claim is reviewed in real-time before the return is filed. The focus is on fixed price contracts with large supply dollars and prototypes. They also closely review acquisitions. Each Business Area maintains its own documentation.

After a few questions, Peter closed the meeting reminding members that the next Roundtable meeting will be in February.