

# 2017 R&D TAX CREDIT- OVERVIEW OF REAL-TIME DATA COLLECTION

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## *The benefits of changing the existing method in 2017*

### *Executive Summary*

#### **2016 METHOD**

ABC Co Tax Department and outside consultants will conduct interviews with Subject Matter Experts (“SME”) in January through March to learn more about 2016 R&D activities and related expenses. Several major projects will be selected for additional investigation. Write-ups (covering Tax Code requirements) will be prepared by Tax Department and Consultants to support selected projects but not all projects will be covered by write-ups. Quantitative work (calculations) will be done by April and qualitative work (write-ups) scheduled to be complete by May/June. This has been the existing method for the past few years.

#### **TRANSITION PLAN**

Meetings will be conducted with SME leadership to discuss the benefits of real-time data collection and to solicit feedback on proposed methods and roll-out of new method and process. The Tax Department and new vendor (“MASSIE”) are flexible in how the new process will be designed and will be going through an architecture phase at that time. SME requirements will be gathered and additional design will occur prior to launch in Summer 2017.

#### **2017 METHOD**

Method is designed to automate the data and documentation gathering in real-time so that SMEs provide more detailed information regarding all material projects as they take place during the year. Possible timing means SMEs would receive an information request for data and documentation in Summer 2017 and be asked to provide activity and cost details for Q1/2 of 2017. 2017 is transition year. January – June might be the first reporting period, and July-December the second reporting period. Goal is to do quarterly gathering in 2018.

#### **REAL-TIME METHOD-BENEFITS**

Method designed so overall time commitment by SMEs stays the same as existing method, but communication between the Tax Department and the SMEs is more frequent. Benefits include SME documentation of more projects, better details of activities provided by SMEs due to timing of inquiries, possible increase of number of projects resulting in a larger credit, more accurate estimates of credit throughout the year, lower vendor costs, better documentation for IRS examination. Tax Department has done due diligence on this method and several large corporations have successfully launched this process already and have achieved the benefits outlined. Now that the R&D tax credit is a permanent part of the Tax Code and President-elect Trump has stated the credit is an incentive that he wants to survive any impending tax reform, this is a good time for ABC to move to real-time data collection.

## What is Real-Time Data Collection

Real-time data collection is not an instant transfer of data from SMEs to the Tax Department. The process refers to periodic data gathering at set intervals throughout the year rather than gathering data all at once the following year. The table below is an example of possible data gathering periods for 2018. With 2017 being the transition year, 2018 will be the first full year of quarterly gathering.

<b>YEAR 2018</b>	<b>Information Request Distributed to SMEs</b>	<b>Data Return Period</b>	<b>Tax Review Finalized</b>
Q1	April 1-5	April 5-30	May 15
Q2	July 1-5	July 5-30	Aug 15
Q3	Oct 1-5	Oct 5-30	Nov 15
Q4	Jan 1-5	Jan 5-30	Feb 15

In this example, SMEs will receive Information Requests within five days after each quarter closes (typically via email) and will have until the end of the distribution month to provide answers to the Tax Department. Information Requests will be designed like interview questions asking SMEs about activities performed related to R&D projects during the previous quarter. SMEs may forward the Information Requests to direct reports to fill out as appropriate. An example question might read:

*Below is a list of projects you provided in Q4 2017, please fill in the name of any new vendor(s) hired during the quarter who assisted your team with R&D-related services. Provide a brief explanation of what the vendor was engaged to do for your team and how they performed or supported R&D activities. If known, please provide the state where the vendor performed the work, if known, and please make a note in the box if you know the work was performed overseas. Please fill in the blanks for new projects added during the quarter.*

<b>PROJECT NAME</b>	<b>NEW Q1 VENDOR(S) NAME</b>	<b>NEW VENDOR(S) ROLE</b>	<b>STATE WHERE VENDOR PERFORMED WORK (IF KNOWN)</b>
<i>SORTING LOOP</i>			
<i>PACKAGE EXPRESS</i>			
<i>REL 4.2</i>			
<i>NEW (new project name if applicable)</i>			

Here is how an SME might have responded to that question:

*Below is a list of projects you provided in Q4 2017, please fill in the name of any new vendor(s) hired during the quarter who assisted your team with R&D-related services. Provide a brief explanation of what the vendor was engaged to do for your team and how they performed or supported R&D activities. If known, please provide the state where the vendor performed the work, if known, and please make a note in the box if you know the work was performed overseas. Please fill in the blanks for new projects added during the quarter.*

<b>PROJECT NAME</b>	<b>NEW Q1 VENDOR(S) NAME</b>	<b>NEW VENDOR(S) ROLE</b>	<b>STATE WHERE VENDOR PERFORMED WORK (IF KNOWN)</b>
<i>SORTING LOOP</i>	<i>Concurrent Computer</i>	<i>Deliver software to run automation in Louisville Hub</i>	<i>KTY</i>
<i>PACKAGE EXPRESS</i>	<i>n/a</i>		
<i>REL 4.2</i>	<i>n/a</i>		
<i>NEW (REL 4.3)</i>	<i>Reliant</i>	<i>Designed new test software</i>	<i>India</i>

A follow up question to the Vendor identification might ask the SME to upload a copy of any new vendor statement of work (“SOW”) and would provide the SME with a secure link to drag and drop the document. In the alternative, SMEs might be asked to identify where the Vendor SOW was kept or who might have access to the contract if further review was needed.

The Information Requests will be optimized so that questions can be answered via cell phone, tablet or PC. Generally sent via email, these requests are designed so that SMEs or their designate will click a secure link to take them to a cloud-based reporting system (no log-in or password required). All Information Requests can be started and saved and the SME will receive an email with a link designed to allow them to continue at a later point in time. Information Requests will be Beta Tested prior to sending to SMEs. This process allows actual SMEs to provide feedback on the format and types of questions asked prior to distribution of the form to a wider SME group. Answers provided during the Beta Test period will be provided to all SMEs in a custom guidebook with FAQs which will accompany each Information Request email. The vendor will provide Help Desk functions related to the Information Requests and step-by-step videos. SME education on the new system is very important and will be rolled out each year to SMEs to communicate any changes in the system, and to educate new SMEs to the method.

In cases where SMEs would prefer to schedule live interviews in lieu of completing the quarterly Information Request, the vendor will be available to schedule those. In the email there will be a link to an on-line calendar so that SMEs can select a convenient date and time with the vendor. Interviews will then take place via an on-line meeting portal like WebEx or Go-To-Meeting so that the vendor can show their screen with the Information Request questions and the SME can also share the screen if they have data or other documentation they would like to explain further.

### **Real-Time Data Collection Benefits**

The LB&I division of the IRS has recently reorganized its workforce and will be examining large taxpayers via issue-focused campaigns beginning in 2017. Common tax return abuse areas will be the primary areas the examination process will cover including the R&D tax credit. The IRS anticipates campaigns to be very focused on facts and circumstances of R&D activities being performed by taxpayers claiming the credit and wants those facts to be very developed by providing contemporaneous documentation supporting the claims. For ABC this means moving to a system or process where all major projects are documented. The real-time data collection process will provide SMEs more opportunities to transfer knowledge quarterly related to R&D activities. This should allow the Tax Department to uncover more R&D activities thus increasing the potential credit each year and provide better documentation based on SME involvement in the process.

In the past the ABC process required SMEs to be interviewed and then the Tax Department and outside consultants participated heavily in writing up the interview notes into documents called "write-ups." Write-ups are designed to outline the activities performed during the year that qualify for the R&D tax credit for each project. The IRS has been known to ask for write-ups for projects based on materiality of the project to the overall R&D tax credit. Some taxpayers, however, have been subject to IRS examination whereby write-ups were asked for all projects included as part of the credit. The new real-time data collection process will allow SMEs to assist in the documentation of activities quarterly, as the year progresses, so that information provided is not only more detailed, it is provided more often. This should allow the write-ups for each project to provide more data than obtained during the current method, and wider coverage of projects.

The conference room interview process has been around since the R&D tax credit was put in the Tax Code in 1981. For many years this was the only method to transfer information because face-to-face interaction was required. As modern technology such as cell phones, the internet, on-line portals, web-tools and other interaction programs such as WebEx and Go-To-Meeting have been invented, the conference room interview has been replaced. The real-time data collection method will allow SMEs to respond to inquiries on their own time. As emails are received, SMEs can pick and choose times that are convenient to them to respond, or can designate other team members or direct reports to respond for them. Questions are cloud-based so they can be answered via cell phone, tablet or PC. This allows SMEs more ways to respond, in their own environment. For SMEs more comfortable with face-to-face interviews, that method will also be available.

Under existing interview methods, SMEs are expected to review prior year projects and notes and familiarize themselves with the activities and costs that were incurred in the prior year before attending the conference room interview. The real-time data collection process is designed so that SMEs can open the quarterly Information Request and begin responding to questions immediately because the facts are fresh on their minds. Memories of activities from a year ago fade out over time. Other companies have found quarterly data capture to be very successful and easier on the SMEs despite more frequent interaction with the Tax Department. For example, if an SME would typically spend 30 minutes preparing for an interview, one hour in the interview, and another 30 minutes answering follow up questions, the total investment would be 2 hours for each SME. Moving to a quarterly system where data and documentation is gathered via cloud-based information gathering would be designed for SMEs to complete each quarter in less than 30 minutes. The goal is for the investment of time by the SME is to improve quality and depth of information, which should result in smoother IRS examinations.

## Frequently-Asked Questions

**How often will SMEs be required to respond to Information Requests?** The plan is to cover 2017 with two requests and move to quarterly requests in 2018.

**How will SMEs know the length of answers that should be provided to questions?** Questions are Beta Tested in advance using a test group of SMEs. Sample answers provided during the Beta Test will be provided as samples for all SMEs in custom guidebooks, or step-by-step guides, issued with each Information Request.

**Will the SME responses be reviewed?** Absolutely. Our new vendor will review all responses and seek clarification of answers with SMEs as needed. The Tax Department will have access to all SME responses as well.

**How much time with the SME need to respond to each Information Request?** The goal is to design the questions whereby SMEs can respond in 30 minutes or less. Once the initial 2017 Information Request has been designed the Beta Testing process will measure the time for each SME and will publish the average time to respond in the guidebook.

**Why are we moving to the new method of real-time data collection?** We believe the new system will be easier on the SMEs allowing them to respond to questions via cell phone, tablet or PC. SMEs will also assist in documenting activities and costs quarterly which should uncover more R&D activities than before and in greater detail. This reporting should also provide the IRS with better information and wider coverage for projects in terms of contemporaneous documentation required to support the projects. The IRS is moving toward issue-focused examinations for R&D tax credits and the Tax Department is anticipating more documentation requests from them in the future.

### About MASSIE R&D Tax Credits

Jason Massie, CPA, Esq. is the President and Founder of MASSIE R&D Tax Credits. He has over 28 years of experience in leading Big Four accounting firm and national law firm practices in this area. Jason is a thought-leader and frequent speaker on R&D tax credits. He on the faculty of the BNA Bloomberg R&D Tax Credit Symposium held annually in Washington, D.C. and is a requested presenter on R&D and IRS controversy with TEI groups around the country. MASSIE R&D Tax Credits is a leading provider of federal and state R&D tax credit services. The Company focuses only on the R&D tax credit and uses best practices to ensure projects are of the highest quality. MASSIE R&D Tax Credits is based in Atlanta, GA, and facilitates a quarterly R&D Tax Credit Roundtable for some of the largest taxpayers in the country to share best practices related to R&D tax credit process.

