MASSIE R&D Tax Credits
Experience Best Practices

TEI Portland White Paper

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Table of Contents

Next Roundtable: June 24, 2026 | 11 AM PT

Our Message to YOU

We want to thank the TEI Portland Chapter members and their leadership for inviting us to speak on such a timely topic. We know it isn't easy balancing your day job with being a TEI leader, so we recognize Brittany Giles and Kim Gill; each of them a joy to work with and helped make the event a success.

During the webinar, we covered important topics like the new Form 6765, cases, controversy, and technology that impact R&D tax credits. If you have questions as you review this white paper, please contact info@massietaxcredits.com, and we will be glad to guide you.

The research credit landscape has entered a period of significant transformation. Between evolving IRS enforcement strategies, heightened documentation expectations, and the introduction of Form 6765 Section G requirements, companies must adapt their R&D tax credit processes to meet new compliance standards. This whitepaper synthesizes key insights from MASSIE R&D Tax Credits and Mayer Brown on how to navigate these changes while optimizing internal processes through modern technology.

Ins and Outs of the R&D Tax Credit for 2026

Jason Massie, MASSIE R&D Tax Credits, Founder & President

OBBBA and State 174 Conformity

We received a question before the Webinar from Jeff Davis of Zion's Bancorporation regarding state conformity with OBBBA for section 174. As such, we have attached many charts from the Council on State Taxation ("COST") that were prepared by that group as of October 31, 2025. Please see the Zoom Toolbar in the Resources area for that handout.

State R&D Tax Credit Landscape

Currently, 39 states offer R&D credits that can be claimed in addition to the federal credit. While many state credits align closely with federal requirements, some states have implemented unique provisions and incentives that require careful attention.

Recent State Developments

Several states have recently enacted significant legislation affecting their R&D credit programs:

- Connecticut expanded and enhanced R&D credits under H.B. 7287, effective June 30, 2025. Single-member LLCs may now qualify if they meet specific size and manufacturing criteria.
- California introduced a new Alternative Simplified Credit election starting with 2025 tax years, allowing 3% of QREs over 50% of the prior three-year average.
- Iowa repealed its former Research Activities Credit and replaced it with a more stringent application program effective for 2026, restricting eligibility to specific industries such as advanced manufacturing and bioscience.
- Michigan enacted a new state R&D tax credit.
- Minnesota made its R&D credit partially refundable beginning in 2025, with refundability set at 19.2% for 2025 and increasing to 25% for 2026-2027.
- Oklahoma created the R&D Rebate Fund and Program through S.B. 324, offering a 5% rebate on QREs capped at $20 million per fiscal year.
- Texas consolidated its R&D incentives into a single franchise tax credit effective January 1, 2026, increasing the credit rate to 8.722% with an enhanced 10.903% rate for university-based research.
- Virginia R&D tax credits have expired for taxable years beginning on or after January 1, 2025.

New Wage Classification Requirements

Form 6765 is undergoing its most significant redesign in years. Section G, which requests business component-level reporting, is optional for tax year 2025 but becomes mandatory for tax year 2026. The IRS opened draft instructions for feedback through March 31, 2026, signaling that this reporting structure will continue to evolve. Companies must now report the top 80% of QREs across no more than 50 business components, ranked in descending order by QRE amount.

For each business component, taxpayers must identify the type (product, process, software, technique, formula, or invention) and provide detailed breakdowns of qualified research expenses including wages by job function.

Form 6765 requires the addition of new wage classification categories. Companies must now identify when individuals are performing Direct Research, Direct Supervision, or Direct Support. These classifications link directly to the experiments, uncertainties, and activities performed and are likely to influence how IRS exam teams evaluate claims. Teams will need clear strategies for defining business components and documenting related activities and costs.

Business Components and Activity-Level Information

The IRS is focusing more heavily on the connection between the activity level of individuals and the qualified research they perform. Documentation should clearly demonstrate which business components generated the most QREs, how activities satisfied the four-part test, how the process of experimentation was carried out, and which individuals performed which activities.

Business components should be defined at an appropriate level of granularity. A business component that is too broad, such as defining an entire automobile as a single component rather than breaking it down into engine systems, electronics, or battery technology, will not provide the level of detail the IRS expects. Companies should consider their product development lifecycle and identify natural breakpoints where qualified research activities occur.

The Critical Role of Documentation

Interviews continue to be useful in supporting the factual record, but recent cases reinforce that interviews alone do not satisfy the burden of proof. Courts have repeatedly emphasized the need for contemporaneous documentation demonstrating technical uncertainty and experimentation

Lessons from Kyocera

The Kyocera case serves as a stark example of the consequences of insufficient documentation. The multinational manufacturer filed a 2018 claim of $400,000, later amended after a PwC study to $1.7 million. The IRS filed a motion for summary judgment, arguing there was no genuine issue of material fact and that the law supported their position since Kyocera bore the burden of proof.
The court found that Kyocera failed to retain technical documentation supporting their credit claim. Subject matter expert testimony provided to PwC was deemed unreliable since it was gathered after the fact.

The court also determined that SMEs opined on an unreasonable number of employees, activity-level information was insufficient to prove the 80% substantially-all threshold, and business components were too broadly defined. Nearly all projects were disallowed.

Key Takeaways from Kyocera

- Documentation must take precedence over interviews
- SMEs must provide opinions on a reasonable number of employees
- After-the-fact testimony is not considered reliable
- Activity-level information and documentation are needed to prove the 80% substantially-all test
- Technical documentation must be retained contemporaneously
- Business components must be appropriately defined with sufficient granularity

IRS Enforcement Update: Changes Impacting R&D Examinations

Paul DiSangro, Partner, Mayer Brown

The IRS enforcement landscape for research credits has undergone significant changes. Large Business & International has been reduced by approximately 25%, Appeals has been downsized by 27%, and the former DOJ Tax division has been reduced by 30%. The IRS has experienced turnover of six Commissioners and four Chief Counsels in recent years, with much of the management structure currently operating in acting or vacant positions.

Enforcement specifically related to R&D has also been impacted. Many engineers hired by the IRS were employed for less than 1 year before being terminated, and the MITRE contract, which provided technical analysis support, has also been terminated.

R&D Examinations Without MITRE

Under the old IRS playbook, examiners would perform minimal work on the four-part test while MITRE would fail projects under one or more of the high threshold of innovation tests. Notices of Proposed Adjustment would simply reference the MITRE report. In 2025, the IRS has generally been dropping the research credit issue in cases where MITRE support is unavailable.

After 2025, the enforcement approach remains unclear, but it is likely that agents will resume examinations using non-fact-intensive arguments such as insufficient substantiation, disallowing sampling methodologies, relying solely on documentation without considering interviews, and not accepting affidavits from researchers.

IRS Litigation Strategy

IRS Counsel has developed a clear playbook for research credit litigation. The strategy involves selecting taxpayers with unfavorable facts—such as those with amended returns, service providers, questionable studies, or credits under $1 million—and litigating against them. The goal is not only to win cases but also to obtain judicial opinions that ratchet up the tests taxpayers must meet, which can then be used to extract better settlements from all taxpayers.

This strategy has proven effective. The IRS has won 11 of the last 14 cases litigated since 2019. Notable decisions include Little Sandy Coal, which established stricter process of experimentation requirements, and Kyocera, which emphasized documentation over testimony.

Fast Track Settlement Program

The Fast Track Settlement program allows taxpayers and exam teams to mediate with an Appeals Officer serving as mediator. While the program fell into disuse, a July 2025 LB&I memo now mandates that teams agree to participate in Fast Track or provide an explanation to the Deputy Commissioner of LB&I.

Fast Track offers several advantages: it is completed within 120 days, uses an informal process, considers hazards of litigation, can be pre-packaged, allows Appeals to influence exam teams, and permits taxpayers to proceed to regular Appeals if unsuccessful. However, exam teams must agree to the final settlement, and if teams are unwilling to compromise, Fast Track becomes ineffective.

Research credits are particularly well-suited for Fast Track because projects can be qualified or disqualified individually, or QREs can be adjusted by percentage based on hazards of litigation. First movers in this space are experiencing success because both LB&I and Appeals want the program to succeed in a resource-constrained environment.

R&D Controversy: Real-World Examination Examples

Stephen Whiteaker, Director of Controversy, MASSIE R&D Tax Credits

Over the past nine years since retiring from the IRS, the landscape of research credit examinations has become significantly more aggressive. The IRS now requires substantial documentation to substantiate credits, and the agency has become emboldened by its success in recent litigation.

Case Study 1: Fast Track That Failed

A client contracted with a foreign entity to build a first-in-industry machine to their specifications, including delivery and installation. The client claimed costs for parts as supplies and treated U.S. oversight of installation and testing as a pilot model. The IRS strongly disfavors pilot model claims.

After limited audit work, the IRS proposed total disallowance based on two positions: first, that the research was funded because the taxpayer was not at risk if the machine failed; and second, that the taxpayer merely purchased a depreciable asset. The exam team was unwilling to compromise during Fast Track mediation, and the process became a waste of time for both parties.

Under the new Fast Track rules, IRS leadership mandates that teams participate or provide explanation to the Deputy Commissioner. However, if teams remain unwilling to compromise, the program will continue to be ineffective. Taxpayers should gauge the exam team's willingness to compromise before agreeing to Fast Track and consider productive discussions about potential settlement parameters beforehand.

Case Study 2: The Consequences of Inadequate Documentation

A taxpayer filed a 2024 refund claim covering 2019 and 2020. The claim was pulled for examination, keeping the statute open for 2019. Initially, the IRS indicated they would not examine the research credit, but in the interim the IRS hired new engineers who needed training cases. Unfortunately, this claim was selected as a training case.
The IRS assigned one engineer to each year—an unprecedented approach. The client refused to push back on IRS requests out of fear, creating additional challenges. Subject matter experts had left the company, records did not exist, and the company had been purchased by a foreign entity.

The IRS proposed 100% disallowance due to the taxpayer's inability to prove qualified research expenses and meet the four-part test. The IRS engineer was unprofessional during the closing conference and stated that nothing the taxpayer said would change his determination. The client declined to elevate the issue, declined to go to Appeals, and ultimately paid back the entire credit.

Lessons Learned

- Do not be afraid to elevate legitimate concerns about audit conduct
- Ensure you have contemporaneous records that substantiate the credit
- Estimating credits and relying on after-the-fact interviews will no longer suffice in an audit

Case Study 3: Success Through Proper Documentation

A large taxpayer underwent examination of their 2019 return but had retained documentation of their research credit activities. Subject matter experts remained on staff and could speak in detail about the work performed. Additionally, the client maintained JIRA data showing individual activities performed and their connection to specific business components.

This examination concluded with a reasonable level of disallowance. The majority of the adjustment related to internal use software, which typically faces a higher bar in examinations due to the three additional tests beyond the standard four-part test: the software cannot be commercially available, it must be intended to result in substantial and economically significant improvements, and the project must involve significant economic risk.

It is important to note the distinction between technical risk and business risk. Business risk, such as funding delays or inadequate training, does not qualify. During examinations, taxpayers should expect to meet these heightened standards for internal use software claims.

Best Practices for Audit Readiness

To be prepared for a successful examination, companies should maintain documentation that clearly defines business components, ties activities to those components, defines technical uncertainties, and documents the process of experimentation used to resolve those uncertainties. Examples of valuable documentation include design documents, technical drawings, test results, emails, meeting notes, and project tracking data.

Tax departments should coordinate with engineering and IT teams to ensure contemporaneous records are retained and can be produced if the company is audited. The IRS is actively looking to disallow credits based on lack of documentation, a much easier case for them than engaging in deep technical arguments.

Optimizing Your R&D Tax Credit Process Using Technology You Already Own

Peter Green, CEO, MASSIE R&D Tax Credits

Modern research credit compliance depends on integrating existing collaboration tools into processes that are intuitive for SMEs and structured for tax teams. Companies increasingly expect to manage R&D documentation within platforms they already use.

The Shift Toward Better User Experience

After interviewing and studying over 200 of America's top companies, MASSIE identified consistent pain points in traditional R&D credit processes: too much work for tax departments, money left on the table, poor SME interaction and response rates, and inadequate documentation for audit preparedness.

Many companies are rethinking their R&D processes by focusing on user experience first. Teams want workflows that fit how SMEs naturally communicate, simple guidance with examples, video tutorials and visual aids, automated reminders, and dashboards that provide real-time visibility.

Modern Collaboration Tools

Companies are successfully leveraging tools such as Microsoft Teams and Slack for R&D collaboration hubs, Planner tasks with automated reminders, Google Workspace for communication and forms, Power BI dashboards for progress tracking, video libraries with sample responses, and documentation mapping checklists.

Microsoft Teams Example

A customized Microsoft Teams hub can serve as the central collaboration space for R&D credit documentation. Key features include:

- Simple Planner tasks assigned to SMEs with clear instructions and due dates
- Instant messaging for real-time questions and answers
- Video training sessions demonstrating what good responses look like
- Real-time analytics showing project progress by business component
- Customized questionnaires tailored to specific departments
- Documentation mapping that provides checkbox lists of likely supporting documents

When SMEs upload documentation through the collaboration hub, files automatically organize into the proper SharePoint folder structure based on business component and documentation type, eliminating the typical inbox overload tax departments experience.

The User Experience Testing Process

Before rolling out questionnaires to 100 SMEs, companies should conduct user experience testing with five representatives. This testing process involves detailed question review, determining internal terminology, implementing company-specific and industry-specific FAQs, utilizing existing systems and data to eliminate unnecessary questions, and refining language based on feedback. Taking time with five SMEs saves significant time when scaling to 100.

Leveraging Existing Data Sources

Many companies already track data required for R&D credit calculations. JIRA data can provide activity-level information showing which employees worked on which projects, time allocations, and technical descriptions of work performed. Product lifecycle management systems document design iterations and testing protocols. Version control systems like GitHub demonstrate the process of experimentation through commit histories.

Companies should identify these existing systems during the architecture phase and extract data programmatically rather than asking SMEs to recreate information that already exists in structured form.

AI-Powered Documentation

Tax departments are experimenting with internal AI deployed behind the firewall to improve documentation quality, classify technical activities, and structure unstructured engineering data. AI tools can identify patterns in JIRA tickets that indicate experimentation, extract technical uncertainties from design documents, and suggest appropriate business component classifications.

However, companies should be aware of risks associated with AI in R&D credit work. AI should augment human judgment rather than replace it. All AI-generated content should be reviewed by qualified SMEs and tax professionals. The IRS has also begun using AI in their examination process, making it critical that taxpayer documentation is accurate and defensible rather than simply AI-generated narratives.

Results: The 98% Response Rate

In 2025, companies using modern collaboration tools and user-centered design achieved an average SME response rate of 98.43%. This dramatic improvement from typical response rates of 60-70% results from making the process genuinely easier for SMEs.

When the process is easier, greater participation generates larger credits while ensuring smoother audits. SMEs appreciate the simplified approach, tax departments gain visibility and control, and the entire process becomes more efficient and defensible.

The Three-Phased Approach

Phase 1: Architecture
The architecture phase involves finding existing systems that can provide commonly requested data, learning about the product or software development lifecycle, identifying innovation and SMEs, discovering the best methods for user interaction, agreeing on the project plan, and developing collaboration tools customized to the organization.

Phase 2: SME Interaction
This phase focuses on process and tools that make interaction easier and more efficient. As Steve Jobs noted, you must start with the customer experience and work backward into the technology. The SME interaction phase implements custom collaboration tools, provides video guides with sample responses, offers documentation mapping with checkbox lists, simplifies time allocation reporting through existing data sources, and conducts user experience testing before full rollout.

Phase 3: Tax Department Visibility
The final phase ensures tax departments have visibility and control over project progress and final report documentation. Real-time Power BI analytics show completion rates by business component, department, and individual SME. Electronic final reports organize all documentation for smooth audits. Post-project reviews identify improvements for the following year.

Action Steps for 2026
As companies prepare for the 2026 tax year, several action steps can help ensure compliance with new requirements while optimizing internal processes:

- Develop a business component strategy that identifies the top 80% of QREs across no more than 50 components
- Gather product or software development lifecycle documentation showing phases, qualified activities, resources, and supporting documentation
- Establish why SMEs are qualified to provide opinions on business components and employee activities, while keeping the number of employees assigned to each SME at a reasonable level

- Value documentation over interviews by retaining and organizing technical documentation contemporaneously rather than waiting until an examination
- Review your current SME engagement process and identify pain points that reduce response rates or documentation quality
- Evaluate technology tools your organization already owns—such as Microsoft Teams, Slack, Google Workspace, or JIRA—and determine how they can be leveraged for R&D credit compliance
- Conduct user experience testing with a small group of SMEs before rolling out questionnaires or processes to the entire organization
- Consider whether Fast Track Settlement may be appropriate for any ongoing or anticipated examinations, while carefully gauging the exam team's willingness to compromise
- Review state-specific R&D credit changes that may impact your organization's multi-state credit calculations
- Ensure coordination between tax, engineering, and IT departments on documentation retention policies

Conclusion

The research credit environment continues to evolve as the IRS increases its expectations for transparency, documentation, and substantiation of activity levels. Form 6765 Section G requirements, heightened documentation standards following cases like Kyocera, and shifts in IRS enforcement strategies all point toward a more rigorous compliance environment.

However, companies that invest in proper documentation processes, leverage modern collaboration tools, and maintain contemporaneous records will be well-positioned to defend their credits while maximizing their benefits. The key is to make R&D credit compliance easier for SMEs, more transparent for tax departments, and more defensible for examinations.

Organizations should view 2026 as an opportunity to modernize their approach to research credits by using technology they already own, focusing on user experience, and building processes that generate better documentation with less work.
If you are exploring ways to modernize your R&D credit process or stay ahead of IRS expectations, reach out to MASSIE or join our next R&D Best Practice Roundtable for practical insights and peer discussion.