

**MARCH  
2016**

## **The R&D Tax Credit Aspects of Ohio**

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**Ohio Businesses can take advantage of the R&D Tax Credit to offset Commercial Activity Tax (CAT) liability.**

Research and development (R&D) plays an essential role in innovation by bringing ideas to the market, promoting economic growth, creating jobs, and keeping Ohio competitive.

The present article will discuss the R&D tax credit opportunity available for innovative companies in Ohio.

### **The R&D Tax Credit**

Enacted in 1981, the Federal Research and Development (R&D) Tax Credit allows a credit of up to 13 percent of eligible spending for new and improved products and processes. Qualified research must meet the following four criteria:

- New or improved products, processes, or software
- Technological in nature
- Elimination of uncertainty
- Process of experimentation

Eligible costs include employee wages, cost of supplies, cost of testing, contract research expenses, and costs associated with developing a patent. On December 18, 2015, President Obama signed the bill making the R&D Tax Credit permanent. Beginning in 2016, the R&D credit can be used to offset Alternative

Minimum tax and startup businesses can utilize the credit against payroll taxes.

### **Ohio's R&D Credit**

In July 2008, the State of Ohio established a credit for Qualified Research Expenses. The Research and Development Investment Tax Credit provides a nonrefundable tax credit which can be taken to offset Commercial Activity Tax (CAT) liability. The Ohio credit is designed to encourage Ohio's corporations to invest in increased Research and Development activities. The implementation of this R&D Investment Tax Credit ensures that innovative businesses are rewarded for initiating new R&D projects and enabled others to continue budgeting ahead for long-term R&D projects.

Authorized by Ohio Code Section 5751.51, the Ohio R&D tax credit is a nonrefundable tax credit of 7% of Qualifying Research Expenses in excess of the taxpayer's average investment in Qualifying Research Expenses over the past three years on in-house and contractual R&D performed in Ohio. Using the federal definition to determine qualifying research expenditures, businesses calculate their credit based on their average expenditure on R&D for the latest three tax years. Excess credit not used in the taxable year in which it is earned may be carried forward for up to seven years. The R&D tax credit is an effective way to support research and development, which plays a critical role in any innovation ecosystem.

The Ohio R&D Tax Credit equals

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seven percent of the amount of Qualified Research Expenses in excess of the taxpayer's average investment in Qualifying Research Expenses over the three preceding taxable years. A sample calculation is included below:

<b>Sample Ohio R&amp;D Tax Credit Calculation:</b>	
Investment in QREs for Taxable Year	\$600,000
Avg. Investment in QREs for 3 Prev. Years	\$200,000
Net Excess of QREs for Taxable Year	\$400,000
Credit Earned (7%)	\$28,000

The Ohio R&D Credit is nonrefundable. As such, if a business generates more R&D credit than its CAT liability for that year, the excess credit amount must be "carried forward" to future tax years. This "carry forward" can occur for up to seven (7) years from when the R&D Credit was generated. There is no special application and/or approval process for the Ohio R&D Credit.

### **Ohio Third Frontier Initiative**

Ohio Third Frontier is a state-wide initiative committed to transforming the growth of startup and early stage technology companies. Businesses and entrepreneurs have access to a statewide network of resources through this nationally-recognized initiative to help turn great ideas into thriving companies and paying jobs.

Created in 2002, the Ohio Third Frontier is an unprecedented commitment to create new technology-based products, companies, industries and jobs. The \$2.3 billion initiative supports applied research and commercialization, entrepreneurial assistance, early-stage capital formation, and expansion of a skilled talent pool that can support technology-based economic growth. The Ohio Third Frontier's strategic intent is to create an "innovation ecosystem" that supports the efficient and seamless transition of great ideas from the laboratory to the marketplace.

The investment of Ohio Third Frontier resources is guided by the following strategic goals: In targeted areas of technology, the Ohio Third Frontier

seeks to support the growth of existing and emerging industry clusters by:

- Increasing the quantity of high-quality research that has commercial relevance to Ohio companies.
- Expanding access and availability of investment capital to create, grow, and attract technology-based enterprises.
- Growing and nurturing an increasingly experienced pool of entrepreneurial management talent.
- Addressing the technical needs of existing companies pursuing new products and production.
- Contributing to the expansion of a technologically proficient workforce.

The Ohio Third Frontier supports a comprehensive portfolio of program activities that include:

#### **Value Chain Development Advanced Energy Program**

The Value Chain Development Advanced Energy Program supports R&D that addresses the technical and cost barriers to commercialization in Ohio of advanced energy components and systems, with preference to wind, biomass, and energy storage.

#### **Advanced Materials Program**

The Advanced Materials Program supports R&D that addresses the technical and cost barriers to commercialization in Ohio of advanced materials products with preference to polymer and carbon nanomaterials, liquid crystals, and bio-based materials.<sup>i</sup>

#### **Biomedical Program**

The Biomedical Program supports R&D that addresses the technical and cost barriers to commercialization in Ohio of biomedical products, with preference to cardiovascular<sup>ii</sup>, regenerative medicine<sup>iii</sup>, and orthopedics.

#### **Fuel Cell Program**

The Fuel Cell Program supports R&D that addresses the technical and cost barriers to commercialization in Ohio of fuel cell and other advanced energy components and systems.<sup>iv</sup>

### Innovation Ohio Loan Fund

The Innovation Ohio Loan Fund assists Ohio companies in developing next generation products and services in targeted industry sectors by financing the acquisition, construction, and related costs of technology, facilities, and equipment.

### Medical Imaging Program

The Medical Imaging Program supports research and development that addresses the technical and cost barriers to commercialization in Ohio of medical imaging components and systems.<sup>v</sup>

### Ohio Research Commercialization Grant Program

The Ohio Research Commercialization Grant Program supports accelerated Ohio commercialization by small companies awarded selected federal R&D funding.

### Photovoltaic Program

The Photovoltaic Program supports R&D that addresses the technical and cost barriers to commercialization in Ohio of photovoltaic components and systems.<sup>vi</sup>

The project listed below provides an example of the R&D efforts that have been supported and grown through the Third Frontier Initiative.

### STACK Construction Technologies

For most new construction, there is often a lengthy bidding process that occurs before groundbreaking begins. Commercial building trade contractors rely on successful bids to secure jobs. The existing process requires them to download hundreds of blueprints each month and often print massive amounts of documentation prior to measuring and counting. To improve this process, STACK Construction Technologies of Mason, Ohio is developing software solutions to address these problems.

Specifically, STACK has developed software to measure and count using digital files online without having to download them first. This platform enables

the viewer to access fifteen to twenty blueprints at a time on a single screen. Traditionally, a contractor would have to go to each individual project's website and assimilate the blueprints and drawings. STACK's program consolidates the necessary data so that contractors can navigate and evaluate many different projects at once. Once trade contractors have selected the blueprints that they require, the STACK Takeoff program allows them to color-code the blueprints within the web browser, simulating the use of colored pencils on a traditional paper blueprint. The program also automatically calculates the area, distance, and volume of the construction. Once this process is complete, the STACK Estimating tool then tells contractors how much of each material that will be required in order to provide an accurate estimation for project costs. This tool is essential for contractors to complete estimates with sustainable profit margins quickly.

There are currently 26 employees at STACK, a number that is expected to double in the near future as STACK continues to invest in R&D projects to develop new software and improve the performance of its existing offerings. STACK and its software development projects are prime examples of R&D efforts that could generate Qualified Research Expenses which are eligible for the Ohio R&D Tax Credit.

### Conclusion

R&D and innovation encourages continual economic growth in Ohio. There are many R&D tax credit opportunities available for innovative companies in Ohio. The new payroll tax credit aspect of the R&D Credit will significantly benefit many start-ups and small to mid-sized businesses. Specifically, the R&D credit has now been expanded to apply credits in excess of income taxes to FICA tax liability, even if a company was unprofitable and had no tax liability. Taxpayers should be aware of federal and state tax incentives which are available to them to help shoulder the costs of innovation.

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<sup>i</sup> See "The R&D Tax Credit Aspects of Nanotechnology" By Charles R. Goulding, Seann Convey, and Andressa Bonafe.

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RDTS Publishing. Available online at:  
<http://www.rdtaxsavers.com/articles/Nanotechnology>.

<sup>ii</sup> See "The R&D Tax Credit Aspects of Heart Disease" by Charles R. Goulding, Andressa Bonafe, and Charles G. Goulding. RDTS Publishing. Available online at:  
<http://www.rdtaxsavers.com/articles/Heart-Disease>

<sup>iii</sup> See "The R&D Tax Aspects of Regenerative Medicine" By Charles R. Goulding, Andressa Bonafe, and Andrea Albanese. RDTS Publishing. Available online at:  
<http://www.rdtaxsavers.com/articles/Regenerative-Medicine>.

<sup>iv</sup> See "The R&D Tax Credit Aspects of Fuel Cell Developments" by Charles R. Goulding, Andressa Bonafe, and Andrea Albanese. RDTS Publishing. Available online at  
<http://www.rdtaxsavers.com/articles/Fuel-Cell>.

<sup>v</sup> See "The R&D Tax Aspects of Brain Mapping" By Charles R. Goulding, Andrea Albanese, and Charles G. Goulding. RDTS Publishing. Available online at  
<http://www.rdtaxsavers.com/articles/Brain-Mapping>.

<sup>vi</sup> See "The R&D Tax Aspects of Photovoltaic Development" By Charles R. Goulding, Andrea Albanese, and Andressa Bonafe. RDTS Publishing. Available online at  
<http://www.rdtaxsavers.com/articles/Photovoltaic-Developments>.