

DON'T OVERLOOK  
THE R&D TAX  
DEDUCTION

2019 STATE OF THE UNION: BE  
PREPARED FOR THE UNEXPECTED

HOUSING FORECAST  
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# Building Savvy



Art Burdick, from left, Alexia Herber,  
Robert Reyes and Monika Morris

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**March 2019**

San Antonio's Homebuilding Industry Publication

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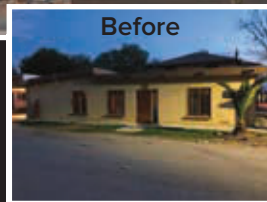


[savvy finance]

# DON'T OVERLOOK THE R&D TAX DEDUCTION



TAXES



## DIAMOND MASONRY

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**Every home build has its challenges. You may be faced with building on less than optimal land or within unique city or county requirements.**

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By Steven Bankler, CPA

Maybe you've been challenged to build stronger, lighter, faster, or more environmentally friendly, energy efficient, or automation-enabled. Perhaps the architectural design of the home is unique and requires outside-the-box building techniques or materials. Or maybe you're building near an Interstate and have a new idea for sound-proofing.

These challenges often require innovation on your part to overcome, which may qualify you for special tax credits. The opportunity falls under Research and Development (R&D). It's not an obvious match for builders and others in the construction industry who don't consider themselves scientists or inventors but, with recent changes, it's becoming a clear tax saver.

In 2015, the federal R&D tax credit was made permanent, which was an important move because it meant businesses could finally

count on the tax credit not expiring abruptly from year to year. As of 2016, qualified small businesses (QSB) can use the credit to offset payroll taxes instead of income taxes, which is also a great advancement. These decisions were made to encourage U.S. companies to innovate—so go ahead and dream big!

That being said, the rule is entangled with other tax requirements and can be difficult to follow. At the most basic level, your R&D needs to fulfill what the IRS considers Qualified Research Activities. To get a better idea of what this means, consider these four rules:

1. The purpose of the activity must be to develop a new or improved product or process in the U.S. That “product” could be a new technique or construction method.
2. The activity needs to involve a hard science like engineering, physics, chemistry, or computer science. Be open-minded here: It’s likely your R&D fits into one of these categories.
3. Some technical uncertainty is necessary (called the Section 174 test). In other words, the activity needs to be true trial and error for which you’re unsure what the result will be.
4. An evaluation of different alternatives needs to be completed either through systematic trial and error (trying alternatives and documenting results) or through modeling and simulation.

The U.S. Department of Treasury reports that, in recent years, nearly 70 percent of qualified research spending among corporations

and individual taxpayers goes toward wages and salaries. About 15 percent is claimed for supplies and another 15 percent is claimed for contract research expenses. For home builders, these expenses could translate into the cost to both employ and contract with individuals to conduct R&D activities and also into the cost of building materials and other supplies necessary to conduct the research.

These R&D costs are deducted at specific rates and other restrictions apply. There are also different IRS forms that need to be filed depending on your business structure and/or whether you’re applying the deduction to offset payroll taxes versus income taxes. Given these factors, it’s important to consult a tax advisor to help you determine exactly how much of your R&D activities can be deducted, how to go about conducting those activities in order for them to qualify, and what forms to file when. ▼

*Steven Bankler has more than 40 years of experience in the accounting industry. Steven’s expertise lies in consulting, planning, tax, and asset protection as well as exit strategy services for closely held businesses. He also provides litigation support (both as a testifying expert witness and a consulting expert), business negotiations and estate planning. For past Building Savvy tax tips and to learn more about Steven Bankler, CPA, Ltd., visit [www.bankler.com](http://www.bankler.com).*

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