Research & Experimentation
Tax Credit Studies
for the Plastics Manufacturing Industry
“I have found working with Mueller Prost to be a very rewarding experience. They are thorough, thoughtful, consummate professionals who bring a strong understanding of manufacturing to their tax work. They have made it their business to fully understand the unique details and characteristics of the R & E Tax Credit, and how the benefits of this tax law can create tax credit opportunities for firms/owners in the plastics industry. I recommend them without reservation.”

Tom Duffey | President, Plastic Components, Inc.
Board President, MAPP

The Research and Experimentation Tax Credit

The R&E tax credit has been in existence since 1981, but recent regulations have relaxed the definition of qualified research activities. Consequently, many companies that were not eligible in the past may now take advantage of this federal tax credit. Due to this change, companies may file amended tax returns to obtain refunds of previously paid income taxes. In some cases, companies may recapture taxes paid up to four years ago.

The R&E tax credit is a wage-based tax credit available for the development or improvement of products, processes, techniques, formulas, inventions or software. In addition to qualified wages, companies may capture supply costs for prototypes, as well as 65 percent of contracted labor spent performing qualified research on behalf of the company. This tax credit is available to all entities filing a federal tax return. In addition, several states offer a modified R&E tax credit.

Companies can benefit by both deducting the research expenditures and by claiming the credit. While the research expenditures are a reduction of taxable income, the R&E tax credit is a general business credit, and a dollar-for-dollar reduction of tax.

The R&E credit is 20 percent of the company’s qualified research expenditures in excess of a base amount. Companies must first use the credit to offset tax for the year the credit is generated. However, if additional credit remains, the company may carry the credit back one previous tax year or forward to the next 20 years.

The Federal R&E tax credit expires periodically, and Congress renews the R&E tax credit annually. The current law allows taxpayers to claim Federal R&E tax credits for expenditures paid or incurred prior to December 31, 2014. Taxpayers may amend Federal tax returns to claim R&E tax credits in prior years and establish systems to claim R&E tax credits in the future. Further, some states have a R&E tax credit program, as well, and may be eligible to claim credits in states in which they perform qualified research.
Requirements

There are **four basic requirements** for research activities to qualify:

1. Qualified research activities are defined as the development or improvement to a business component, which is defined as a product, process, technique, formula, invention or software.

2. The research must be technological in nature. That is, the process of experimentation used to discover the information fundamentally relies upon the physical or biological sciences, engineering or computer science. Furthermore, companies may use existing technologies and may rely upon existing principles to satisfy this requirement.

3. The research must be intended to eliminate uncertainty concerning the development or improvement of a business component. Uncertainty exists if the capability or method for developing the business component is unknown, or if the appropriate design of the business component is unknown.

4. Elimination of the technical uncertainty must be accomplished through a process of experimentation, including systematic trial and error, modeling or simulation.

Research & Experimentation Checklist: *Do You Qualify?*

*Do you...*
- Improve customer part designs to improve manufacturability?
- Design tools, jigs, molds or dies?
- Develop prototypes or models (including computer-generated models)?
- Apply for patents?
- Test new materials?
- Conduct testing of new concepts and technology?
- Develop new technology?
- Test new concepts or technology?
- Implement robotics or production control software?
- Streamline or improve production or manufacturing processes to achieve higher standards in quality and productivity?
- Perform certification testing?
- Add new equipment?
- Expend resources on outside consultants or contractors to conduct any of the above-stated activities?

*If you answered “yes” to any of these activities, you may qualify!*
Frequently Asked Questions

Is this something new?
The R&E tax credit has been in existence since 1981, but recent regulations have relaxed the definition of qualified research activities. Consequently, many companies that were not eligible in the past may now take advantage of this federal tax credit. Due to this change, companies may file amended tax returns to obtain refunds of previously paid income taxes. In some cases, companies may recapture taxes paid up to four years ago.

How will this affect my existing relationship with my tax advisor?
The R&E Tax Credit is a highly specialized area, and our team works with your current tax advisor. While your current tax advisor is fully capable, they are not likely specialists in the complex R&E Tax Credit area. Our specialists are willing to coordinate the delivery of the R&E study with your tax/CPA firm. We are not in competition and are not looking to replace any existing relationship. Mueller Prost’s R&E Tax Credit Group just wants to help you maximize your R&E tax credits.

How long before I realize the cash benefit from this study?
Refunds are typically issued between 90 and 120 days after filing. However, if your credit reduces a tax balance currently due (i.e. estimated tax payments), the benefit is immediate.

What is the time commitment from my team?
The exact amount depends on your company’s structure, the available documentation, and the extent of your company’s R&E expenditures. Typically, personnel from your finance, engineering and R&E areas should anticipate spending some time with our consultants.
Common Myths About the R&E Tax Credit

“Our business is simple and not ‘high-tech.’ We probably don’t qualify.”

If you are developing new processes or products, or improving existing processes or products, you may qualify. If you have devoted resources to evaluating a new technology, investigating new materials, improving machinery or tools, developing and implementing lean manufacturing techniques or improving the environmental impact of your processes, you may be eligible.

Industries Claiming Credits
(Source: Joint Committee on Taxation Calculations from the Internal Revenue Service, 2005)

“We are a small company. This credit is just for big business.”

There is no size requirement for the R&E credit. Both large and small companies are potential candidates for the credit. If you have new or improved processes or products, you may be eligible for the credit.

Size of Companies Claiming Credits by Total Assets
(Source: Joint Committee on Taxation Calculations from the Internal Revenue Service, 2005)
Common Myths About the R&E Tax Credit, cont’d.

“We’ll just tell our CPA to file the right form at the end of the year to receive the credit.”

Successfully documenting the R&E tax credits to which you are entitled is more complicated than just filing the appropriate form. Highly specialized knowledge of current and historical requirements, along with determining and documenting qualified activities and compiling supporting documentation are necessary to substantiate and defend your claim.

Mueller Prost has studied the intricacies of IRC Section 41 and has the technical knowledge necessary to identify activities that qualify for the credit. Additionally, our team of professional engineers and accountants possess the skills necessary to help your company develop and implement a process for tracking and documenting the necessary information to sustain credits.

Our process includes a plant tour and interviews with your key management. Along with other documentation, these are both necessary to substantiate your credit. However, because of our experience, we have streamlined our process to minimize the disruption of your operations.

Our interviews are designed to capture all eligible costs and appropriate documentation in the most efficient and direct way possible.

“Our CPA looked into this a few years ago. We didn’t qualify.”

Recent legislation has expanded and simplified the credit eligibility so many additional taxpayers can receive these credits. In fact, unclaimed credits from prior years also can be recovered under the current legislation.

This recent legislation has also led to an increased emphasis on compiling source documentation to support the credit claim. A review of this documentation allows our team to qualify projects and differentiate between qualifying and non-qualifying activities.

This documentation, compiled with our team’s assistance, includes documents supporting:

- Qualified wages
- Supplies consumed during experimentation, and
- Contract labor
Our Five-Phase Engagement Process

PHASE 1: INITIAL MEETING - NO CHARGE
Our process begins with a meeting between the professionals of Mueller Prost and the management team of the Company. At this time, an overview of the credit and its scope are presented. After this meeting, Mueller Prost and the management team identify employees performing qualified activities. This enables Mueller Prost to identify important areas of opportunity as they relate to the Research and Experimentation Credit. Also at this time, we discuss the Company’s contemporaneous documentation with management and determine whether it is beneficial to proceed with the calculation.

PHASE 2: PRELIMINARY ASSESSMENT - NO CHARGE
After discussing the guidelines of the Credit with the management of the Company, and discussing the necessary documentation to support a Research Credit claim, Mueller Prost determines the potential qualifying research and experimentation expenses for each period for which credits are available.

PHASE 3: DOCUMENTATION AND SUPPLEMENTAL INTERVIEWS
After identifying the general areas of activities eligible for the credit, the contemporaneously prepared research documentation is reviewed with management. Research documentation, such as research reports, drawings, pictures, meeting minutes, design development notes, email correspondence, experimentation results, documents supporting time spent, and research notes, demonstrating specific support of the qualified nature of the Company’s activities, is vital to the support of the credit claim. Interviews are then conducted with those employees that played a role in the research and experimentation activities. These employees that performed the research are excellent sources of detail regarding the research activities of the Company, and corroborate the contemporaneously prepared research records. These employees also identify the uncertainties, challenges, improvements, and developments of the eligible business components.

PHASE 4: CALCULATE AND SUBSTANTIATE THE CREDIT
Based on the documentation and the interviews and meetings with the employees performing the research, Mueller Prost assists the Company in compiling the underlying support of the credit claim, which includes research reports, drawings, pictures, meeting minutes, design development notes, email correspondence, experimentation results, documents supporting time spent, and research notes. Mueller Prost also provides the Company with a credit calculation for each period covered by the Study. This supporting documentation and calculation serves as a basis for your credit claim.

PHASE 5: PLANNING FOR THE FUTURE
After the initial study is complete, Mueller Prost’s goal is to assist you in claiming future research credits. This step includes discussing improvements to documentation, capturing the time applicable to research and experimentation, and recording information with respect to testing and functionality. Mueller Prost will assist you in developing a system for capturing the necessary information to support the tax credit.
Mueller Prost’s R&E Tax Credit Group

The R&E Tax Credit Group specializes in assisting manufacturers and their advisors in maximizing the R&E tax credit (IRC § 41).

More clients choose our Tax Credit Group over other firms for several reasons:

- Our group specializes in IRC § 41 exclusively and relies on these regulations as the basis for your tax credit results.
- Our team members’ professional backgrounds consist of tax, financial, engineering, operational and technical sales; we know how to ask the right questions, and understand your business.
- Our assistance in identifying and gathering source documents to support the credit claim.
- We have streamlined our own processes to provide the highest quality service, with the least interruption to your operation.
- We make it our priority to research your industry, company and operation prior to beginning our fieldwork.
- We are backed by our solid reputation as a CPA and business advisory firm that has been in operation since 1983.

Case Studies

<table>
<thead>
<tr>
<th>Project Description</th>
<th>Savings</th>
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<tbody>
<tr>
<td>$ 8 million Custom plastic injection molder</td>
<td>$ 145,000 in savings</td>
</tr>
<tr>
<td>$ 90 million Proprietary products injection molder</td>
<td>$ 362,000 in savings</td>
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<tr>
<td>$ 15 million Custom plastic injection molder</td>
<td>$ 125,000 in savings</td>
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<tr>
<td>$ 20 million Custom plastic injection molder</td>
<td>$ 350,000 in savings</td>
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<tr>
<td>$ 2 million Tool &amp; die shop</td>
<td>$ 80,000 in savings</td>
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<tr>
<td>$ 5 million Tool &amp; die shop</td>
<td>$ 275,000 in savings</td>
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What Our Clients Are Saying...

“A large regional CPA firm reviewed our operations and estimated a potential R&E tax credit benefit of $60,000 for a four year period. After talking with Mueller Prost and utilizing their specialized knowledge of our industry, operations and the tax credit, our savings were $382,000 over that same period.”

- A $50 million metal enclosure manufacturer

“We had three of the Big 4 CPA firms look at our tax returns for the past three years. These firms’ local representatives once told us we had taken all eligible R&E credits. We then had Mueller Prost review our returns and our complex business operations. They helped us identify previously overlooked qualifying expenditures and previously unclaimed credits. These credits were subsequently audited by the IRS without change. We are deeply indebted to Mueller Prost’s R&E expertise and understanding. They are truly experts in this area.”

- An $800 million durable goods manufacturer

“Our local CPA firm and several large national and regional CPA firms advised us that we were entitled to $25,000 of annual R&E credits. Mueller Prost reviewed our prior returns and helped us identify significantly more qualifying R&E expenditures. These additional R&E credits resulted in more than $750,000 in refunds from prior years, previously overlooked and unclaimed. They also identified another $600,000 in tax savings overlooked by the other firms. This was a very beneficial study.”

- A $150 million consumer products manufacturer
Selected Members of Our Team

**Douglas M. Mueller, CPA**
President & Founding Partner

Doug Mueller has been nationally recognized by the *Wall Street Journal* and *Money Magazine*, where he frequently contributes tips on wealth management, protection, and high-level tax strategies. For more than 25 years, Doug has focused his practice on working with high net worth clients and structuring assets to minimize tax liabilities. Doug is currently known internationally for his expertise on the Research and Experimentation Tax Credit, and is a highly preferred speaker on this subject for professional organizations nationally. He is a member of the American Institute of Certified Public Accountants and the Missouri Society of CPAs. He also serves the St. Louis Community as a member of various charitable and business-related boards.

**Adam J. Herman, CPA/ABV/CFF, CVA, ASA, CFE**
Partner and Director of Consulting Services

Adam Herman has focused his more than 21 years of experience on serving the special needs of businesses and their owners. He provides consulting and support services in the areas of business valuation, litigation services, merger and acquisition services, research and experimentation (R&E) tax credit services and business operational analysis. As director of the fast-growing R&E Tax Credit Group at Mueller Prost PC, Adam has led nationwide engagements resulting in substantial tax savings for manufacturing companies as well as a variety of other companies in several industries. As a highly sought-after speaker on a national and regional basis for professional organizations, he is also the Chairman of the Legal Services and Business Valuation Committee for PKF North America, an association of more than 100 mid-sized U.S. accounting firms, and a member of many renowned regional and national organizations. In addition, Adam is currently serving as the co-chairman of the National R&E Roundtable Group. These activities contributed to Adam being named to the 40 Under 40 Class of 2007 by the *St. Louis Business Journal*.

**Michael J. Devereux II, CPA, CMP**
Partner and Director of Manufacturing & Distribution Services

Mike Devereux joined the firm in 2000 as a tax consultant and business advisor. As an energetic and ambitious accountant with an outstanding passion for tax, Mike has demonstrated leadership and exceptional judgment in the tax structuring of various acquisitions and has led hundreds of R&E Tax Credit study engagements, and is lead coordinator for Mueller Prost PC’s special tax incentives program. He is frequently asked to speak to various professional and industry trade organizations and associations about opportunities to reduce federal and state tax liability. Mike is a member of the AICPA, MSCPA, and Associated Industries of Missouri. Mike also serves on the Executive Committee for Good Shepherd Children & Family Services, a Catholic Charities agency. These activities contributed to Mike being named to the 30 Under 30 Class of 2007 by the *St. Louis Business Journal*. Mike received his undergraduate degree in accounting from Southwest Missouri State University and is currently enrolled in the Masters of Taxation Program at Fontbonne University.
Douglas A. Kolker, CPA
Director of R&E Tax Credit Group
Doug Kolker has over 10 years of experience running his own small business and more than 12 years of experience in public accounting and consulting. Doug is passionate about helping small-to-mid-size companies stay competitive through the use of various tax credit programs. He has supervised R&E Studies around the country, focusing his efforts in the dental laboratory industry and the custom machine tool industry. Doug is a member of the Missouri Society of CPAs and other community, civic and charitable organizations.

Stephen M. George, PE, CEM
Senior Engineer
As a licensed Professional Engineer, Stephen George brings 25 years of chemical process industry leadership to help manufacturing companies of all types take advantage of their well-earned research and experimentation tax credits. Having lived the fact that American innovation occurs in every facet of an operation - from the shop floor to the Board Room - he is uniquely positioned to help clients identify qualified research activities. His company was a pioneer in the ISO 9000 certification process industries. The documentation process required for ISO is directly related to R&E documentation. His first-hand experience with $100 million plus mergers and acquisitions from both sides of the table is an invaluable asset in effectively describing manufacturing processes. Steve is a graduat of Georgia Tech with a B.S. in Chemical Engineering.
About Mueller Prost

Mueller Prost offers practical solutions and insightful advice to individuals, businesses, and non-profit organizations, providing a full range of audit, tax, accounting, and business advisory services. The experience of our more than 90 accountants, engineers, operations leaders and former business owners gives us a unique and comprehensive perspective to address the needs of growing organizations. In addition, we leverage our membership in PKF North America (an association of more than 100 legally independent accounting and consulting firms) to enhance our national and international capabilities.

For more information, visit www.muellerprost.com

About Mueller Prost’s Tax Credit Group

The research and experimentation tax credit rewards businesses for innovation and improvement to their products and processes.

Mueller Prost’s Tax Credit Group excels at providing research and experimentation tax credit studies to manufacturers, helping them identify activities which qualify for the credit.

For more information, visit www.muellerprost.com/re