

Research and development tax incentives for the automotive industry

Your opportunity

The increased pressure from fuel-efficiency standards, the need to address operational costs, and suppliers' role in developing new content continue to transform the automotive industry and reshape its research and development (R&D) programs.

You can address the cost and risk of research and development (R&D) by leveraging available federal, state, and local tax incentives. Two methods exist to calculate the credit for taxpayers who conduct qualified research: (1) the traditional incremental research credit and (2) the alternative simplified credit (ASC). The ASC is beneficial to companies that have not reported research credits in the past or have reported nominal credits due to the burdensome base amount rules. Whichever credit you choose to explore, it is important to understand the rulings and interpretive guidance since you must be prepared to defend reported R&D tax credits.

various conceptual alternatives to determine the appropriate combination of design variables.

- Developing new product or process test methodologies to evaluate performance and assess feasibility of alternative conceptual designs.
- Designing and fabricating prototypes or tooling.
- Prototype testing of vehicles and components resulting in a new or improved product.
- Developing manufacturing technologies to increase product quality, enhance production throughput, improve cycle time, strengthen manufacturing efficiency, or reduce cost or waste.
- Implementing, evaluating, and validating potential alternative manufacturing process enhancements to improve production capabilities.

Determining the true cost of R&D is often difficult because few companies have a project accounting system that captures many of the costs for support provided by the various personnel who collaborate on R&D. The typical project tracking system would not include contractor fees, direct support costs, and salaries of high-level personnel who participate in the research effort.

Is your company fully aware of opportunities for federal, global, and state research tax incentives?

Federal tax credits provide permanent benefits to drive down effective tax rates and generate cash flow. You also may qualify for state and global incentives, depending on where activities are performed.

Examples of initiatives that may be eligible for R&D tax incentives include:

- Designing and developing new or improved products or manufacturing processes.
- Performing analyses to identify opportunities for product or manufacturing process improvements and testing of

The IRS has designated the research credit as a "Tier One" issue under its Strategic Initiative. Examinations now begin with a standardized "Tier One" Information Document Request (IDR), defining a broader, more intensive test. Moreover, approaches adopted and accepted by the IRS in prior examinations may no longer be accepted. We have carefully monitored this Strategic Initiative in order to address these heightened substantiation requirements. Do you have the documentation needed to comply with these new requirements?

Deloitte can help.

Our approach

The Deloitte R&D team is a national practice of highly experienced tax professionals specializing in R&D tax incentives. Our team includes former IRS and Treasury officials who were integral in developing the statutory provision (§41), regulations, rulings, court cases, and issue papers. We also have an automotive product engineer with extensive experience with a major automotive manufacturer. Additionally, we have environmental and mechanical engineers, scientists, and other professionals with a deep understanding of the issues associated with automotive product and manufacturing process R&D. These specialists can help you identify qualified R&D activities and assemble documentation to defend your claim, based on their extensive knowledge of the law and your industry.

Our R&D professionals are exclusively dedicated to R&D tax issues and specialize in particular industries, including the automotive industry. Our focus provides us with an unusual depth of experience. We also work in an efficient and nonintrusive manner so that you can stay focused on business.

In addition, we have a demonstrated methodology that includes:

Integration of software solutions — Deloitte has created a powerful technology tool, **DBXi**, which helps automate the computation and information-gathering processes associated with R&D credit projects. **DBXi** is a broad, Web-based information management system that provides easy-to-use, activity-based information requests, as well as facilitating the uploading and storage of relevant contemporaneous documentation.

Deloitte will customize a **DBXi** system for your company. Our approach includes system design and setup, training for technical personnel, monitoring of the annual process, assisting with the review and analysis of information, and providing a detailed review of the annual documentation and computation process.

Quality Assurance — Our Quality Assurance team reviews deliverables and computations to evaluate whether the research credit rules are properly applied and that the full scope of qualifying research is considered. This team includes former senior officials with the IRS, Treasury, and

Congressional staff who participated in drafting the legislation and regulations, as well as developing current IRS test policies and practices. To help evaluate compliance, our process includes a pre-inspect of your claim by former IRS revenue agents with vast experience with R&D checks.

R&D tax studies — Our R&D tax studies address federal research tax credits and deductions, as well as global and state R&D incentives. We report to you at the end of each phase of our study so that you can determine if you wish to proceed with the next phase. If our initial scoping phase indicates that a full study is not justified, you may elect to terminate the study. If you want us to proceed with a full study, we perform indepth fieldwork and prepare the documentation needed to support our findings. Additionally, we can provide support during the IRS examination of your claim.

Our goal is to provide value beyond the R&D tax incentives that you claim. Our approach provides a process that your tax function can replicate and use to manage future compliance costs and burden.

The Deloitte difference

The Deloitte R&D team provides you with the comfort of knowing that you have fully considered tax incentives that can impact R&D costs. We offer:

- Extensive experience providing services to Fortune 1000 automotive companies and their suppliers, vendors, and contractors.
- A demonstrated methodology for carefully evaluating and documenting R&D tax incentives.
- A national team with deep technical knowledge in this complex area.
- Proprietary software, tailored to your circumstances.
- An automotive product engineer with extensive experience with a major automotive manufacturer to assist in the development of documentation.
- Other specialists, including environmental and mechanical engineers and scientists who understand automotive companies' qualified research.
- Efficient and nonintrusive R&D analyses that help you stay focused on business.

