

Anchin Alert

Anchin, Block & Anchin LLP
Accountants and Advisors



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IRS Emphasizes the Need for Compliance When Claiming Tax Credits

This past February, the IRS released its annual “**Dirty Dozen**” list of warning alerts for 2016 filing season. The Dirty Dozen includes a variety of common scams taxpayers may encounter at any time during the year. The items on this year’s list are:

1. Identity Theft
2. Phone Scams
3. Phishing
4. Return Preparer Fraud
5. Hiding Money or Income Offshore
6. Inflated Refund Claims
7. Fake Charities
8. Falsely Peddling Deductions
9. *Excessive Claims for Business Credits (includes research credits)*
10. Falsifying Income to Claim Tax credits
11. Abusive Tax Shelters
12. Frivolous Tax Arguments

Included within excessive claims for business credits are research tax credits. Claiming excessive business credits, whether intentionally or not, by improper calculation of qualified expenses is dangerous. Two schemes, in particular, have drawn attention from the IRS for the upcoming filing season: fraud involving the fuel tax credit AND fraud involving research tax credits. Of all available research tax credits, the federal Research & Development (R&D) tax credit is the largest and most commonly claimed. Since its inception in 1981, the R&D credit has been temporary, but the recently passed Protecting Americans from Tax Hikes Act (PATH) of 2015 has now made it permanent and more accessible to many taxpayers ([please see our Anchin Alert from December 21](#)).

The IRS is understandably concerned about the increasing number and cost of claims along with the related increase in abuse. They are warning taxpayers that in addition to wasting time, effort and resources, unsupported claims for tax credits will likely lead to penalties and interest payments. Improper claims generally involve failures by the taxpayer to prove participation in or adequately substantiate qualified research activities and/or satisfy other IRS requirements.

The R&D tax credit is intended to benefit U.S. companies who develop new or improved products or processes through technical research and experimentation that leads to an elimination of design or development uncertainty. The credit is applicable not only to revolutionary innovations but company specific evolutionary advances as well. Numerous industries are eligible including: semiconductors, software, life sciences, engineering, energy, chemicals, apparel, and food science just to name a few. Increasingly, business management teams have recognized the importance of taking advantage of this generous federal incentive as a powerful weapon for remaining competitive and refueling their critical innovation engines.

While the IRS is focused on finding taxpayers that are abusing the credit, it is important for **any taxpayer claiming the credit to strictly adhere to IRS guidelines in calculating the amount of the credit and collecting contemporaneous documentation to support it.** In order to minimize the taxpayer's time, cost, and efforts associated with claiming R&D credits, it is imperative that each taxpayer claiming an R&D credit has a comprehensive study completed by qualified professionals to ensure that their claim is proper and substantiated adequately. A strong R&D credit claim requires employee interviews, documentation of qualified activities in the tax year (and careful base period construction for first time claims). The product of this exercise, should be a written study that clearly matches the taxpayer's qualifying R&D activities with the tax law. The report is essential in memorializing the qualifying nature of projects and activities performed, and establishing nexus for particular scientists and engineers.

While the rules and applications can be complex, Anchin's Research & Development Tax Credits practice employs tax experts and engineers who can work with you to determine if your company qualifies for the R&D credit, estimate the expected range of benefit, and deliver a professional, accurate and sustainable R&D tax credit claim that your company will be proud of – credibility is critical and we believe our product will help you benefit from the tax credit to which you are entitled.

For more information, contact Yair Holtzman, Partner and Practice Leader of Anchin's Research & Development Tax Credits practice at yair.holtzman@anchin.com or 914.860.5599.

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