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THE R&D PAYROLL TAX CREDIT:

A Start-Up's Secret Weapon

The idea was the easy part. The funding is the hard part.

If you're a growing start-up and have little or no income tax liability, you might benefit from the R&D Payroll Tax Credit. Eligible firms can use the Credit to increase capital by offsetting payroll tax, and the maximum claim amount was recently doubled. However, it's a limited-time opportunity, so the thoughtful entrepreneur must seize the day.

ELIGIBILITY

- Only "Qualifying Small Businesses" (QSBs) are eligible
- QSBs have: No more than 5 years of revenues AND
- Less than $5M in gross receipts for the current tax year
- Especially useful for QSBs raising seed funding, or in Series A or Series B funding rounds
- Ideal for pre-profit start-ups with high burn rates, though profitable QSBs can claim it too
- CPEOs may claim the Credit on behalf of a QSB client

BENEFIT

- Credit was established as part of the R&D Tax Credit by PATH Act in 2015, but benefit was boosted by IRA in 2022
- For tax years beginning after 12.31.2022: Claim up to $500K annually
  - May use to offset FICA or Medicare payroll tax liability
- For tax years prior to 12.31.2022: Claim up to $250K annually
  - May only be applied to FICA
- May be taken before and during the first 5 years of revenue
- Can be used by a pass-through entity to ease complexity
  - If the non-Payroll R&D Credit is taken, the benefit will pass through to the shareholders
  - If the Payroll Credit is taken, the benefit will be used to offset payroll and stay in the company, eliminating the need to transfer or reapportion benefit

TIMING

- Must be included on a timely filed return – no amending allowed
- It can only be claimed in the first 5 years of revenues – and the clock starts ticking as soon as any amount of revenue is accrued. Even interest in a bank account is enough to start the 5-year countdown

EXAMPLE SOFTWARE TECHNOLOGY FIRM, COLORADO, TY 2023

- Launched in 2020, pre-revenue
- Qualified Wages: $3,048,363
- Qualified Computer Rental Costs: $140,346
- Total QREs: $3,188,709
- Federal Tax Credit: $318,871

EXAMPLE CIVIL ENGINEERING FIRM, PHOENIX, TY 2023

- Launched in 2023, $450K in revenues
- Payroll: $800,242, of which $500,000 were qualified expenses
- Total QREs: $500,000
- Federal Tax Credit: $48,000

EXAMPLE CONSUMER PRODUCT DEVELOPMENT FIRM, MANHATTAN, TY 2023

- Launched in 2022, minimal revenues
- Qualified Wages: $200,000
- Qualified Contractor Expenses: $100,000
- Total QREs: $300,000
- Federal Tax Credit: $25,000

CONTACT ME

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Capstan Tax Strategies delivers engineering-driven specialty tax solutions that maximize the valuable tax benefits of real estate holdings. By complementing and collaborating with accounting firms, we arm commercial real estate owners, executives, and tenants with the data and analysis required to accelerate depreciation, maximize deductions, and capture tax credits.

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