

# FINANCIAL PERSPECTIVE

## BREAKING GROUND ON TAX SAVINGS: A CFO'S GUIDE TO BUILDING YOUR COMPANY'S R&D TAX CREDIT

BY ROSS ALESSANDRO

### Introduction

In construction, innovation is everywhere – from new building techniques to advanced project management software. Yet, many construction companies overlook a powerful financial incentive: the Federal Research & Development (R&D) Tax Credit. This credit isn't just for tech giants, manufacturers and pharmaceutical companies; it's designed to reward any company investing in new processes, technologies, or solutions – including those in construction. Recent legislative changes have made the credit even more accessible, and understanding how it's calculated can help CFOs unlock substantial tax savings.

This article provides an overview of the Federal R&D Tax Credit, highlights recent developments, and offers practical guidance for construction CFOs seeking to maximize their company's tax savings and reinvest in growth.

### Background: The R&D Tax Credit – A Brief History

The R&D Tax Credit, formally known as the "Credit for Increasing Research Activities" under IRC Section 41, was introduced in 1981 as part of the Economic Recovery Tax Act (ERTA). Its purpose: to encourage domestic innovation by providing a dollar-for-dollar reduction in federal tax liability for qualified research activities (QRAs). Over the years, the credit was extended 16 times, reflecting its importance to U.S. economic policy. In 2015, the Protecting Americans from Tax Hikes (PATH) Act made the credit permanent and expanded its benefits, allowing eligible start-up companies to offset payroll taxes – meaning some taxpayers don't even need to be in a taxable position to benefit.

The methodologies for calculating and documenting the credit have evolved, but its core mission remains: to reward companies that invest in innovation. Some examples of potential QRAs in the construction industry include the following:

- Developing schematic and structural designs
- Design and development of new roads, bridges, dams or other civil structures
- Evaluating designs provided by architects or engineers for constructability and identifying potential design improvements during estimating
- Evaluating alternative materials to improve designs or meet specific project requirements
- Developing new or improving existing designs to achieve LEED and green building initiatives
- Evaluating engineering and construction methods to improve performance, reliability, quality, or function

- Designing and engineering unique material transfer or construction systems to accommodate space restrictions on site
- Designing and engineering temporary support structures used during project implementation
- Conducting geotechnical and environmental analyses to evaluate land suitability and serve as a design input
- Redesigning or retrofitting antiquated structures with modern, energy-efficient systems
- Testing and commissioning of mechanical, electrical, and/or plumbing (MEP) systems

In addition to the "traditional" construction industry QRAs listed above, there are many potential QRAs related to software development and A.I. activities in the construction industry, including the following:

- Developing or customizing project management, scheduling, or cost estimation software tailored to unique construction workflows
- Creating or enhancing Building Information Modeling (BIM) platforms or integrations
- Designing A.I.-powered tools for predictive maintenance, safety monitoring, or resource allocation on job sites
- Implementing machine learning algorithms to optimize construction sequencing, logistics, or material usage
- Developing automated quality control systems using computer vision or sensor data
- Integrating A.I. with drones or robotics for site surveying, progress tracking, or hazard detection

These activities often involve technical uncertainty, iterative testing, and the application of engineering or computer science principles – all hallmarks of qualified research under the R&D Tax Credit.

### Qualifying for the Credit: The Four-Part Test

To claim the R&D Tax Credit, construction firms must show their activities meet the IRS's Four-Part Test:

1. Permitted Purpose: Improving a business component's function, performance, reliability, or quality.
2. Technological in Nature: Based on engineering and/or the physical, material, and computer sciences.
3. Elimination of Uncertainty: Addressing uncertainty in capability, method, or design.
4. Process of Experimentation: Evaluating alternatives through modeling, prototyping, or trial and error.

## How the Credit Is Calculated

The R&D Tax Credit is based on “Qualified Research Expenditures” (QREs) – the money spent on eligible research activities. QREs typically include:

- Wages for employees directly involved in R&D
- Payments to third-party contractors for R&D work
- Supplies used in the research process

## The Alternative Simplified Credit (ASC) Formula

There are two main calculation methods: the **Regular Credit** and the **Alternative Simplified Credit (ASC)**. Most companies use the ASC because it’s simpler and doesn’t require extensive historical data.

The ASC is calculated as follows:

$$\text{Credit} = 14\% \times (\text{Current Year QREs} - \text{Average QREs for Prior 3 Years})$$

If the company has no QREs in any of the prior three years, the credit is 6% of current year QREs.

## Hypothetical Example: Large Construction Company

Let’s say “ABC Construction” undertook several qualifying activities in 2025, including:

- Developing schematic and structural designs (QREs: \$4,000,000)
- Developing and testing a new temporary support structure for a complex urban build (QREs: \$3,000,000)
- Evaluating alternative materials and commissioning new MEP systems for a retrofit (QREs: \$5,000,000)
- Developing or customizing project management, scheduling, or cost estimation software tailored to unique construction workflows (QREs: \$2,000,000)
- Designing A.I.-powered tools for predictive maintenance, safety monitoring, and resource allocation on job sites (QREs: \$2,000,000)

Total QREs for 2025: \$16,000,000

QREs for prior years:

2022: \$6,000,000

2023: \$7,000,000

2024: \$8,000,000

### Step 1: Calculate the average QREs for the prior three years:

$$\text{Average QREs} = (6,000,000 + 7,000,000 + 8,000,000) / 3 = \$7,000,000$$

### Step 2: Subtract the average from the current year’s QREs:

$$16,000,000 - 7,000,000 = \$9,000,000$$

### Step 3: Multiply by the ASC rate (14%):

$$\$9,000,000 \times 0.14 = \$1,260,000$$

**Result:** ABC Construction would be eligible for a \$1,260,000 federal tax credit for 2025.

## What Does This Mean for Your Company?

- The credit is a dollar-for-dollar reduction in federal tax liability.
- Unused credits can be carried forward up to 20 years.
- For start-ups and small businesses, the credit can offset payroll taxes (up to \$500,000 annually for up to five years).

## Recent Developments:

### Legislative Changes and Opportunities

The landscape for R&D incentives has shifted dramatically in recent years. The Tax Cuts and Jobs Act (TCJA) of 2017 initially required companies to capitalize and amortize research expenditures, reducing immediate tax benefits. However, the passage of the One Big Beautiful Bill Act (OBBBA) in July 2025 restored the ability to immediately expense domestic research and experimental (R&E) expenditures under new IRC Section 174A.

## Key Provisions for Construction CFOs

- **Immediate Expensing Returns:** For tax years beginning after December 31, 2024, domestic R&E costs are fully deductible in the year incurred—no special election required.
- **Retroactive Relief for Small Businesses:** Companies with average gross receipts of \$31 million or less over the past three years can amend 2022–2024 returns or take a catch-up deduction in 2025 (or split it between 2025 and 2026).
- **Accelerated Deductions for Larger Businesses:** Firms above the small business threshold can accelerate remaining amortization from 2022–24 over one or two years starting in 2025.

Foreign research expenditures must still be capitalized and amortized over 15 years, but for most domestic construction projects, the new rules mean faster tax savings and improved cash flow.

## IRS Guidance and Documentation

The IRS has issued new guidance (Rev. Proc. 2025-28) outlining procedures for making elections under the OBBBA. Additionally, Form 6765 – the primary vehicle for claiming the R&D credit – has been revised to require more detailed information, including:

- Number of business components and officer’s wages included as QREs
- Detailed breakdowns of QREs by business component and type (required for 2026)
- Exemptions for companies with QREs ≤ \$1.5 million and gross receipts ≤ \$50 million

Robust documentation is now more important than ever. Construction CFOs should work with their tax advisors to implement R&D tracking systems and maintain contemporaneous records.

### Why Construction Companies Should Care

Despite its name, the R&D Tax Credit is not just for scientists in lab coats. In construction, innovation happens on the job site, in the design office, and in the boardroom. By leveraging the credit, CFOs can:

- Reduce federal tax liability, freeing up capital for new projects
- Offset payroll taxes for start-ups and small businesses
- Improve competitiveness by reinvesting savings in technology and talent
- Demonstrate a commitment to innovation to clients and stakeholders


### Practical Steps for CFOs

1. **Identify Potential QRAs:** Review recent and ongoing projects for activities that meet the Four-Part Test.
2. **Engage Project Teams:** Educate engineers, architects,

and managers about qualifying activities and documentation requirements.

3. **Implement Tracking Systems:** Use project management software or dedicated R&D tracking tools to capture eligible expenses.
4. **Consult Tax Advisors:** Work with professionals experienced in construction R&D credits to ensure compliance and maximize benefits. While the credit can be carried forward for up to 20 years, the statute to claim the credit is generally open for only three years.
5. **File Timely and Accurately:** Complete Form 6765 with your original tax return and maintain supporting documentation.

### Conclusion

Innovation is the foundation of progress in construction. The Federal R&D Tax Credit offers CFOs a strategic opportunity to reward ingenuity, improve financial performance, and build a culture of continuous improvement. With recent legislative changes making the credit more accessible, now is the time for construction companies to take action. By understanding the rules, documenting activities, and claiming the credit, CFOs can help their firms break new ground – both on the job site and on the balance sheet. 



# LET'S BUILD A SOLID FINANCIAL FOUNDATION.

100 PINWOOD LANE, SUITE 201 | WARRENDALE, PA 15086  
(724) 934-5300 | hbkcpa.com

 **HBK**<sup>®</sup>  
CPAs & Consultants

WORKING TOGETHER SETS US APART