

Research and Development Credit – Cloud Computing Expenses – Are You Missing Out?

The Research and Development Tax Credit (R&D) has adapted over the years as technology has changed, in order to address new costs and expenses related to the qualified expenses. One of these areas in which there has been significant change over the past decade is in the realm of software development, due to the fast-paced nature of the industry and the speed at which new techniques and processes are implemented. Case in point, one of the commonly accepted expenses claimed by software developers in the past were the cost of licenses for software development tools utilized by developers specifically for qualified development activities. These costs were commonly classified as “supply” costs, as it could be argued that the nature of the expense was something necessary to and “consumed” within the development. Additionally, the definition of “Supplies” included the stipulation that the item be “any tangible property,” which could be construed to mean the physical copies of software (CDs, etc.) that were commonly provided by the creator of the software development tool.

However, as technology has changed, and most software is now either delivered digitally via download or through a subscription-based model (i.e., Adobe Creative Cloud), there is literally no longer a “tangible property” component, and therefore **a much higher risk factor in claiming these licensing expenses as supply Qualified Research Expenses (QRE).**

While this concept may seem to reduce the potential QRE a software development company may be able to claim, in looking at the changing landscape, technology and methods in the software development arena, an increasingly common cost is the use of cloud-based resources such as Amazon Web Services (AWS) or Microsoft Azure. At their beginning, many of these cloud-based services were utilized mainly as an off-site storage solution. However, as these companies have continually developed their platforms and integrated tools designed specifically for developers, many software companies are using these services for actual development activities. In doing, so the costs associated with these services can and have been successfully claimed under the banner of computer rental QRE.

Computer Rental

Computer Rental is defined in §41(b)(2)(A)(iii) as “any amount paid or incurred to another person for the right to use computers in the conduct of qualified research.”

A developer can take advantage of cloud-based command-line tools and software development kits (SDKs) to deploy and manage applications and services. For example, the AWS Command Line Interface is Amazon's proprietary code interface. A developer can also use AWS Tools for Powershell to manage cloud services from Windows environments and AWS Serverless Application Model to simulate an AWS environment to test Lambda functions. AWS SDKs are available for a variety of platforms and programming languages, including Java, PHP, Python, Node.js, Ruby, C++, Android and iOS.

A development team can also create continuous integration and continuous delivery pipelines with services like AWS CodePipeline, AWS CodeBuild, AWS CodeDeploy and AWS CodeStar. A developer can also store code in Git repositories with AWS CodeCommit and evaluate the performance of microservices-based applications with AWS X-Ray.

Technology is continually changing and will continue to do so. As software development companies adapt to and integrate these new technologies and processes, it doesn't have to be at the detriment of losing qualified QRE expenses. Many of these costs have just changed, from "Supply QRE" to Computer Rental QRE." As there is no reduction in direct expenses claimed for computer rental as there are for "Contract Research QRE" (65% reduction), many of these software development companies have been able to realize the same or similar levels of qualified expenses when capturing R&D.