

CLIENT ALERT



May 2010

Qualifying Therapeutic Discovery Project Tax Credit for Small and Medium-Sized Biotech Companies

The Patient Protection and Affordable Care Act (the "Act"), enacted on March 23, 2010, established the Qualifying Therapeutic Discovery Project Credit (the "Credit"). The Credit represents a significant financial benefit to small and medium-sized biotechnology and life sciences companies (must not employ more than 250 employees in all businesses of the taxpayer). The Credit is available in the form of a 50 percent federal income tax credit or cash grant for "qualified investments" necessary for and related to "qualifying therapeutic discovery projects" incurred in a taxable year beginning in 2009 or 2010. The aggregate amount of credits and grants that can be awarded to all taxpayers under the Credit program is capped at \$1 billion. The Credit will have the effect of reducing a qualifying taxpayer's tax liability and, if the taxpayer has no tax liability, it can receive a nontaxable grant for the same amount.

Qualifying Therapeutic Discovery Projects

The Credit is available in the amount of a taxpayer's qualified investment. A qualified investment is the aggregate amount of costs paid or incurred for expenses necessary for and directly related to the conduct of a qualifying therapeutic discovery project. A qualifying therapeutic discovery project is one designed to:

- treat or prevent diseases or conditions by conducting pre-clinical activities, clinical trials and clinical studies or carrying out research protocols aimed at securing Food and Drug Administration approval of a product
- diagnose diseases or conditions
- determine molecular factors related to diseases or conditions by developing molecular diagnostics to guide therapeutic decisions
- develop a product, process or technology to further the delivery or administration of therapeutics

A qualified investment does not include certain types of costs, such as compensation paid to certain highly compensated employees, interest expenses, facility maintenance expenses (mortgage or rent payments, insurance payments, utility and maintenance costs, and the costs of employing maintenance personnel), certain general and administrative costs, and any other expenses determined to be appropriate by the Secretary of the Treasury (the "Treasury").

Selection Criteria

The Treasury must take into account several factors when apportioning the \$1 billion Credit among competing applicants. In particular, taxpayers will need to show that a project has a reasonable potential to:

- result in new therapies to treat areas of unmet medical need
- result in new therapies to prevent, detect, or treat chronic or acute diseases and conditions
- reduce long-term health care costs in the U.S.
- significantly advance the goal of curing cancer within the 30 year period beginning on the date the program is established
- create or sustain high quality, high paying jobs in the U.S.
- advance U.S. competitiveness in the fields of life, biological, and medical sciences

Grant in Lieu of Credit

A taxpayer can elect to receive the Credit as a nontaxable cash grant in lieu of a tax credit. This is particularly beneficial for a taxpayer that would not otherwise be able to take advantage of a tax credit because it has no taxable income.

Application Procedures

The legislation provides that the Treasury, in consultation with the Department of Health and Human Services, has until May 21, 2010, to issue Credit application guidance. The Treasury must approve or deny a submitted application within 30 days of submission. Each discrete project will require a separate application. Credit recipients will be identified to the general public. In advance of the release of this guidance, a taxpayer should begin gathering documentation that will substantiate qualified investments and identifying eligible projects.

For more information or assistance in preparing an application, please contact one of the following attorneys in the Armstrong Teasdale Tax Department:

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