



# Alert

Life Sciences and Health Care, Tax Advice & Controversy, and Corporate  
Finance & Securities Client Service Groups

To: Our Clients and Friends

May 1, 2010

## Qualifying Therapeutic Discovery Project Credit

Who Should Review?: All Biotech, Life Science, and Healthcare Companies with 250 or fewer Employees which are Developing Medical Products or Therapies

Urgency: Before May 21, 2010 You Should Determine Whether You Qualify for This One-Time, Federal Stimulus Grant

The new Qualifying Therapeutic Discovery Project tax credit (the "Therapeutic Discovery Credit") may provide significant financial benefits to small and medium-sized (i.e. up to 250 employees) biotechnology and life sciences companies and their investors.

Created by the Patient Protection and Affordable Care Act enacted on March 23, 2010, the Therapeutic Discovery Credit provides \$1 billion in tax credits and grants for expenditures necessary for and related to "qualifying therapeutic discovery projects." The legislation provides that the Secretary of the Treasury ("Treasury"), in consultation with the Department of Health and Human Services ("HHS"), is required to issue guidance for applying for the credit by May 21, 2010.

Under newly enacted Internal Revenue Code ("Code") section 48D, companies may receive, as either a tax credit or a grant, 50 percent of the amount of certain "qualified investments" made in a taxable year beginning in 2009 or 2010. Because the Therapeutic Discovery Credit is payable as either a tax credit or a nontaxable grant, at the election of the applicant, companies that have operating losses and are thus unable to utilize tax credits currently may nevertheless recognize a current cash flow benefit from this program.

### What is a qualified investment?

For purposes of the Therapeutic Discovery Credit, 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," which amount must be certified by Treasury. A qualifying therapeutic discovery project is a project designed to:

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- 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; or
- develop a product, process or technology to further the delivery or administration of therapeutics.

A “qualified investment” includes research costs as well as capital equipment used in a qualified project. It does not include certain types of costs, such as compensation paid to certain highly compensated employees, interest expenses, facility maintenance expenses (which include mortgage or rent payments, insurance payments, utility and maintenance costs and the costs of employing maintenance personnel), certain indirect costs including personnel, data processing and accounting costs, and any other expenses determined by Treasury to be appropriate for exclusion.

### **Who is eligible to receive credits?**

In order to be eligible for the Therapeutic Discovery Credit, a company (in all of its businesses) must employ not more than 250 people at the time it submits its application, taking into account certain aggregation rules that apply to groups of affiliated companies. In addition, certain entities that do not pay federal income tax are not eligible for a grant, including federal, state or local governments (or subdivisions, agencies or instrumentalities thereof), certain tax-exempt organizations and “qualified issuers” as defined in Code section 54(j)(4). Partnerships and other pass-through entities with ineligible partners or members are also not generally eligible to receive grants. The Therapeutic Discovery Credit does not preclude public companies from seeking these credits, so long as the company does not employ greater than 250 persons.

### **What are the limitations on the credit?**

The Therapeutic Discovery Credit legislation provides for certain limitations intended to prevent “double dipping.” These limitations include:

- No deduction is permitted for expenses for which a Therapeutic Discovery Credit is received;
- If credit is given for qualified expenditures relating to depreciable property, the tax basis of that property must be reduced by the amount of the credit; and
- Expenditures for which a Therapeutic Discovery Credit is received will generally be excluded from the determination of the amount of certain otherwise potentially available tax credits (such as those relating to certain research and clinical testing expenditures under Code sections 41 and 45C).

### **How will benefits be awarded?**

Because a maximum of \$1 billion has been appropriated for the Therapeutic Discovery Credit, it will almost certainly be necessary for Treasury to apportion this amount among competing applicants. Code

section 48D directs Treasury to take into account several factors in making these determinations. In particular, companies will need to show that a project has a reasonable potential to:

- result in new therapies to treat areas of unmet medical need or to prevent, detect or treat chronic or acute diseases or conditions,
- reduce long-term health care costs in the United States, or
- advance significantly the goal of curing cancer within the 30-year period beginning on the date Treasury establishes the program.

Treasury is also directed to take into consideration which projects have “the greatest potential (i) to create and sustain (directly or indirectly) high-quality, high-paying jobs in the United States, and (ii) to advance United States competitiveness in the fields of life, biological, and medical sciences.” Code section 48D requires Treasury, in consultation with HHS, to establish a Therapeutic Discovery Credit application and selection program by May 21, 2010, and application forms should be available shortly thereafter. Treasury is required to consider and approve applications within 30 days of their submission.

### **How can Bryan Cave help?**

Although it is not possible to predict with certainty what the application or selection process will entail until Treasury issues guidance, there are several steps Bryan Cave can assist you with now to increase your chances for a successful application. We can assist with:

- assessing your ability to qualify for a credit or a grant under the program;
- assisting your accounting department in preparing qualitative narratives and qualitative data explaining how your company’s projects fit within the Therapeutic Discovery Credit criteria described above;
- assisting you in developing a strategy for optimizing the success of your application;
- consulting with respect to the presentation of the detailed records of qualifying costs from 2009 and budgeted costs for 2010 to support the credit requested and/or to help prepare the draft qualitative narrative in support of the application; and
- assisting you in identifying and reviewing supporting documentation.

On or about May 27, 2010, Bryan Cave will host a Webinar to discuss the Therapeutic Discovery Tax Credit, including strategies for completing the application. Included in this webinar will be guidance from Bryan Cave’s Washington-based experts in tax credits, HHS and life sciences. Watch for a subsequent announcement for Webinar details.

We would be pleased to discuss the impact of this matter on your organization. Feel free to contact any member of the Qualifying Therapeutic Discovery Project Tax Credit Team listed below.

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