



Recent Tax Court Decisions Could Have Material Consequences on Future R&D Credit Claims

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Recently, the Tax Court has ruled or issued orders in three unique cases that could significantly impact the future of R&D tax credit claims. It is critical to understand what these rulings mean, how they impact your current and future claims, and their impact on ongoing audits and appeals.

In *Tangel v. Commr.*, T.C. Memo. 2021-1 (January 11, 2021), Judge Lauber granted the IRS' motion for summary judgment regarding one of the taxpayer's projects because the Court found that the taxpayer's research was funded, because it did not retain "substantial rights" in the research performed.

The tax regulations specify two main factors as relevant in ascertaining whether research is "funded."

1. The taxpayer claiming the credit must bear financial risk, and
2. retain substantial rights in the research.

The Tax Court held that "the taxpayer perform[ed] research under an agreement that confer[red] on another person the exclusive right to exploit the results of the research."

In *Meyer, Borgman, and Johnson, Inc. v. Commr.*, Tax Court Docket No. 7805-16 (2020), Judge Holmes granted summary judgment to the IRS on the issue of whether research expenses were for funded research. Judge Holmes concluded that the research performed by Meyer, Borgman, and Johnson ("MBJ") under various contracts was funded research because payment for the research was not contingent on the success of the research.

In coming to this conclusion, Judge Holmes stated that the "problem for MBJ here is that none of the contracts we examined expressly or by clear implication make payment contingent on the success of MBJ's research." Judge Holmes held that "the payments to MBJ were not contingent on the success of research, and whatever financial risk they imposed on MBJ was not the financial risk that its research would fail. These contracts were funded by MBJ's clients."

In *Little Sandy Coal Co., Inc. v. Commr.*, T.C. Memo. 2021-15 (February 11, 2021), Judge Halpern concluded that the requirement that at least 80% of a taxpayer's research must constitute elements of a POE (process of experimentation) only applies to activities, not to physical components of the product being developed or improved. The Court also held that one who provides services in direct supervision or support of research is not "engaged in" research. It was further held that because supplies are not activities, when the fraction described in Treas. Reg. 1.41-4(a)(6) is computed using costs as a measure of activities, the costs of supplies used in the development of the product are not taken into account.

In this case, the Tax Court denied a research credit claim based on the interpretation of the 80% experimentation test in the regulations governing the research tax credit.

Please join us for a live [Webinar](#) on March 17, 2021, at 1:00 pm EST. We will be discussing these and other relevant cases in detail.

[Contact an A&M Tax and R&D specialist](#) to learn more about these developments. It's more important than ever to ensure you are meeting the criteria.

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