



# TaxNewsFlash

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## U.S. Tax Court: “Qualified research” test under section 41, summary judgment denied

The U.S. Tax Court today released a memorandum opinion denying the government’s motion for summary judgment based on an argument that the taxpayers’ construction designs failed to meet the definition of “business components” that constitutes one of four threshold tests for “qualified research” under section 41.

The case is: *Harper v. Commissioner*, T.C. Memo 2023-57 (May 10, 2023). Read the Tax Court’s [opinion](#) [PDF 174 KB]

### Summary

The taxpayers claimed section 41 credits for tax years 2012 and 2013 in connection with the activities of their S corporation, a design-build company and general contractor that has worked on residential, commercial, and industrial projects.

Section 41 provides a tax credit for certain “qualified research expenses” of taxpayers carrying on a trade or business. Qualified research expenses must be appropriately related to “qualified research,” encompassing activities that meet all of the following four threshold tests: (1) the section 174 test, (2) the technological information test, (3) the business component test, and (4) the process of experimentation test. The section 174 test requires that the expenditures involved in the research qualify as “research or experimental expenditures” under section 174. The technological information test requires that the research be undertaken for the purpose of discovering information of a technological nature. The business component test requires that the taxpayer intend the discovered information “to be useful in the development of a new or improved business component of the taxpayer.” The process of experimentation test requires that substantially all of the activities involved in the research constitute a process of experimentation for a purpose related to performance, reliability, quality, or a new or improved function, but not related to style, taste, cosmetic, or seasonal design factors.

The IRS disallowed the credits claimed by the taxpayers, and the taxpayers filed a petition with the Tax Court. The government moved for summary judgment, alleging that the construction designs that underlie the taxpayers' claims for section 41 credits for increasing research activities failed to meet the definition of "business components" that constitutes one of four threshold tests for qualified research under section 41.

Section 41(d)(2)(B) defines a business component as "any product, process, computer software, technique, formula, or invention which is to be—(i) held for sale, lease, or license, or (ii) used by the taxpayer in a trade or business of the taxpayer."

The Tax Court denied the government's motion, rejecting all of the alternative grounds asserted by the government for finding that the taxpayers failed the business component test. The court specifically concluded that it was irrelevant that the taxpayers' construction designs were not "products" because they could still qualify as processes, techniques, or inventions.

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