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Proposed Tax Legislation Would Permit Immediate Deduction of Domestic R&E Expenditures for Limited Period

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On May 22, 2025, the US House of Representatives passed the "One Big Beautiful Bill Act" (OBBBA), which includes a temporary suspension of the amortization requirement for domestic research and experimentation (R&E) expenditures. Instead, the OBBBA would permit immediate deduction of certain domestic R&E expenditures in tax years beginning after December 31, 2024, and before January 1, 2030.

Historically, Section 174 of the Internal Revenue Code (IRC) permitted immediate deduction of all costs associated with R&E activities. However, as previously discussed in a **May 2023 Cooley client alert**, for tax years beginning on or after January 1, 2022, the Tax Cuts and Jobs Act of 2017 (TCJA) required taxpayers to capitalize R&E expenditures and amortize them over five years for R&E performed within the United States, or 15 years for R&E performed outside the United States. For additional background on Section 174 and the impact of the TCJA on the treatment of R&E expenditures, see this **September 2023 Cooley client alert**.

The capitalization requirement imposed by the TCJA eliminated immediate deduction of R&E expenditures and thereby increased taxable income for many companies in research-heavy industries, such as life sciences and software development. Many such companies, especially those with pre-commercial operations and limited sources of revenue, were surprised to have net taxable income during their research and development (R&D) phase of operations. This issue was particularly acute for life sciences companies that received upfront payments under a licensing or collaboration agreement intended to fund R&D. It had been expected that new legislation would repeal the capitalization requirement entirely and retroactively, but the proposed legislation does not do so. Instead, if it is passed into law, the OBBBA temporarily suspends the mandatory capitalization requirement for certain domestic R&E expenditures.

Under the OBBBA, new Section 174A would permit taxpayers to elect to immediately deduct R&E expenditures incurred in connection with the taxpayer's trade or business for work conducted within the United States or its possessions in taxable years beginning after December 31, 2024, and before January 1, 2030. Deductions for domestic R&E expenditures under Section 174A will be reduced by the amount of any tax credit allowed under Section 41(a) for increasing research activities.

Alternatively, new Section 174A would allow taxpayers to elect to continue to capitalize and amortize domestic R&E expenditures over a period of not less than 60 months as may be selected by the taxpayer (beginning with the midpoint of the taxable year in which such expenditures were incurred), or elect under Section 59(e) to capitalize and amortize R&E expenditures ratably over a 10-year period, beginning in the tax year in which such expenditures are incurred.

Each election made pursuant to new Section 174A would apply to all subsequent taxable years and can only be changed with the approval of the Secretary of the Treasury.

Additionally, under the OBBBA, an amendment to Section 174(d) is proposed to prevent the use of remaining tax basis associated with capitalized R&E expenditures (as either a deduction or an offset to amount realized) in the event the property developed through such expenditures is later disposed of (i.e., continued amortization of such capitalized R&E expenditures would be required even after the taxpayer disposes of the property).

Questions remain about the interaction among Section 174, 174A and other provisions of the IRC, such as the deduction for foreign-derived intangible income under IRC Section 250, global intangible low-taxed income (GILTI) and the foreign tax credit rules. It also is unclear how these proposed changes would impact anticipated guidance that is yet to be issued following the TCJA, such as the treatment of cost-sharing arrangements for research jointly conducted by affiliated entities.

If you have questions about how these changes may impact your company, we strongly suggest contacting a member of the Cooley tax team, your accountant or other tax advisor.

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