

Modified LB&I directive addresses revised effective dates for ‘temporary repairs regulations’

April 11, 2013

In brief

The IRS Large Business and International Division (LB&I) recently issued a memorandum for all LB&I staff that provides direction to field examiners on the repair versus capitalization issue. The memorandum sets forth modified examination instructions to reflect amendments to the effective date of the temporary tangible property regulations (the temporary repairs regulations).

In detail

Background

The temporary repairs regulations, issued on December 23, 2011, generally are effective for tax years beginning on or after January 1, 2012. The regulations provide broad guidance for expenditures related to tangible property, including materials and supplies, de minimis amounts, acquisition and production of new units of property, and dispositions of tangible property. The regulations also provide guidance on accounting for amounts deducted in accordance with a taxpayer's book capitalization policy (the de minimis rule).

LB&I 2012 Directive

On March 15, 2012, LB&I issued LB&I Directive No. LB&I-4-0312-004 (the 2012 Directive)

providing direction to exam teams on examinations of the repair versus capitalization issue. The 2012 Directive applied to exam activity relating to positions taken on original returns relating to the following issues:

- Whether costs incurred to maintain, replace, or improve tangible property must be capitalized under section 263(a), and
- Any correlative issues involving the disposition of structural components of a building or dispositions of tangible depreciable assets (other than a building or its structural components).

The 2012 Directive did not apply to current examination activity relating to (1) costs for which the IRS provides specific

guidance, separate from the temporary repairs regulations, for determining whether expenditures incurred to maintain, replace, or improve tangible property must be capitalized under section 263(a), or (2) issues that do not pertain to whether costs incurred to maintain, replace, or improve tangible property must be capitalized under section 263(a). This limitation includes specific guidance related to, for example, railroad track maintenance; wireless network asset maintenance; the transport, delivery, and sale of electricity; changes from impermissible to permissible methods of account for depreciation or amortization; and materials and supplies.

Tax years beginning before January 1, 2012

Regarding the examination of tax years beginning before January 1, 2012, the 2012 Directive instructed the field to discontinue current exam activity with regard to the issues covered by the 2012 Directive, and not begin any new exam activity with regard to those issues. However, the 2012 Directive added that if a taxpayer files a Form 3115, Application for Change in Accounting Method, with regard to those issues on or after December 23, 2011, for a tax year not covered by the temporary repairs regulations, field examiners should "risk assess" the Form 3115 and determine, in consultation with the Change in Accounting Method Issue Practice Group, whether to examine the Form 3115.

This risk assessment should include consideration of whether the taxpayer's section 481(a) adjustment properly accounts for amounts paid to acquire, produce, or improve tangible property that were computed under the taxpayer's prior method and previously deducted under section 162; a determination of whether the section 481(a) adjustment resulting from any prior-year change was taken into account; and consideration of the accuracy of the section 481(a) adjustment.

Tax years beginning on or after January 1, 2012, and before January 1, 2014

For tax years beginning on or after January 1, 2012, but before January 1, 2014, the 2012 Directive instructed examiners to determine whether the taxpayer filed a Form 3115 in accordance with the applicable guidance. If the taxpayer has filed a proper Form 3115, the examiner should perform a risk assessment regarding the method change. If the taxpayer has not filed a Form 3115,

and the taxpayer still is in its first or second tax year beginning after December 31, 2011 (the waiver period), the examiner should not examine the issues and allow the taxpayer until the end of the waiver period to file Form 3115. If the taxpayer has not filed Form 3115 and the waiver period has expired, then the examiner should perform a risk assessment regarding the issues.

Tax years beginning on or after January 1, 2014

The 2012 Directive provided that examinations of tax years beginning on or after January 1, 2014, should follow normal exam procedures.

Notice 2012-73

On November 20, 2012, the IRS published Notice 2012-73, announcing its intent to delay the effective date of the temporary repairs regulations to 2014, to publish final repairs regulations in 2013 (effective in 2014), and to modify portions of the temporary repairs regulations related to de minimis amounts, dispositions, and the routine maintenance safe harbor.

On December 14, 2012, the IRS published regulations amending the temporary repairs regulations to delay the effective date of the regulations as announced in Notice 2012-73. The temporary repairs regulations generally are effective for tax years beginning on or after January 1, 2014, with certain portions effective for costs incurred in tax years beginning on or after January 1, 2014.

For more information on the temporary repairs regulations and Notice 2012-73, please see WNTS Insight, "[The tangible property repair regulations: effective dates, units of property, and dispositions](#)," January 4, 2012; WNTS Insight, "[The tangible property repair regulations: acquisition or improvement of](#)

[property](#)" January 5, 2012; WNTS Insight, "[The tangible property repair regulations: plan of rehabilitation, environmental remediation, rotable spare parts, general asset accounts, removal costs, and recovery of certain capital improvements](#)," January 6, 2012; WNTS Insight, "[IRS issues guidance related to final 'repairs regulations' and delay of effective date](#)" November 20, 2012; and WNTS Insight, "[IRS formally delays effective date of the temporary repairs regulations](#)," December 14, 2012.

LB&I 2013 Directive

On March 22, 2013, as a result of the delay in the effective date of the temporary regulations, LB&I issued LB&I-04-0313-001 (the 2013 Directive) to replace the 2012 Directive. The 2013 Directive provides modified examination instructions for tax years beginning on or after January 1, 2012, and before January 1, 2014, while also restating prior examination instructions for tax years beginning before January 1, 2012, and for tax years beginning on or after January 1, 2014.

These modified examination instructions direct field examiners who begin examining a return for a tax year beginning on or after January 1, 2012, and before January 1, 2014, to determine if the taxpayer has changed its method of accounting (with or without filing a Form 3115). If the field examiner determines that the taxpayer has changed its method of accounting, the examiner is directed to perform a risk assessment regarding the method change. If the field examiner determines that the taxpayer has not changed its method of accounting, the examiner is directed not to examine the issue.

The 2013 Directive applies to examinations of original tax return positions relating to costs incurred to maintain, replace, or improve tangible

property, and any correlative issues involving the disposition of building structural components or tangible depreciable assets. However, the 2013 Directive does not apply to examinations relating to costs for which the IRS has provided specific guidance, separate from the temporary regulations, or issues not pertaining to whether expenditures incurred to maintain, replace, or improve tangible property should be capitalized under Section 263(a) (e.g.,

railroad track maintenance and wireless network asset maintenance).

For tax years beginning on or after January 1, 2014, the 2013 Directive instructs field examiners to apply the regulations in effect and to follow normal exam procedures.

related to the temporary repairs regulations. However, the application of the grace period is nuanced. Further, the IRS continues to communicate clearly that taxpayers are expected to adopt the repairs regulations when finalized for 2014.

The takeaway

Taxpayers should be aware that the IRS has formally extended the grace period for examinations of issues

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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