Accounting Methods Spotlight

Recent developments and guidance on tax accounting issues

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This quarter's *Accounting Methods Spotlight* features:

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Did you know…?

Last year, the enactment of the One Big Beautiful Bill Act (OBBBA) reshaped the federal tax landscape for taxpayers across virtually every industry.

Some of what followed was predictable: the Joint Committee on Taxation published its General Explanation of the Act (the "Blue Book"), Treasury and the IRS moved to issue preliminary guidance on key provisions, and taxpayers began the complex work of implementing new elections and method changes. Other developments were anything but expected—most notably, the US Supreme Court's landmark decision in *Learning Resources, Inc., et al. v. Trump, President of the United States, et al.*, invalidating tariffs imposed under the International Emergency Economic Powers Act (IEEPA), which introduced a new set of federal income tax questions for importers seeking refunds.

This edition of the Accounting Methods Spotlight takes stock of where we are today: the guidance that has been issued, planning considerations and novel questions that have emerged, and issues that present risk due to significant uncertainty in the current environment. More than ever, taxpayers are determining the downstream effects of OBBBA on numerous tax attributes, including corporate alternative minimum tax (CAMT) exposure, business interest deductions, charitable contribution limits, research or experimental (R&E) expenditures, net operating loss and foreign tax credit utilization, and foreign-derived deduction-eligible income, global intangible low-taxed income, and subpart F profiles.

Federal income tax considerations of tariff refunds after the IEEPA decision

Following the US Supreme Court's decision related to tariffs imposed under IEEPA, the US Court of International Trade ruled that all importers of record who paid IEEPA tariffs were entitled to relief. While tariff refunds may be welcome news, the unusual nature of the IEEPA tariff litigation and the resulting refund process raises numerous federal income tax questions.

Could tariff refunds generate taxable income?

A tariff refund represents a return of money already paid, rather than new earnings. The federal income tax treatment of tariffs previously paid could differ from ordinary business income, depending on how the original tariff cost was reflected on a taxpayer's return. The characterization of tariff refunds also could affect other tax calculations that depend on whether a payment qualifies as a "gross receipt."

- **What if the tariff cost was previously deducted or recognized as cost of goods sold?** Taxpayers generally have a recognition event when a cost that was previously deducted has been recovered to the extent the previous deduction reduced the amount of the taxpayer's tax liability.
- **What if the tariff cost was capitalized into the cost of inventory or other assets?** Tariff costs generally attach to the underlying goods on which they were paid. If a refund reduces the cost basis

of inventory and other assets (e.g., fixed assets), then it could have ripple effects on cost of goods sold, tax depreciation, tax credits, and other calculations tied to that asset's original cost basis.

- **Could the taxpayer's inventory method affect the outcome?** Different inventory methods (e.g., LIFO versus FIFO) could produce different results when tariff costs are unwound. For instance, the adjustment made by a FIFO taxpayer may be more direct in some cases, but it is not necessarily straightforward merely because inventory turns annually. Outcomes will also depend on the timing of when the tariffs were originally paid, when they were refunded, and whether any of that inventory was still on hand when the refund was recognized. A LIFO taxpayer similarly may need to consider whether the tariffs were charged to cost of sales or reflected in a layer increment in one of the years during which the tariffs were incurred, in which case allocating the refund to different inventory layers may be relevant.

What if tariff refunds are owed or rebated to customers?

Many businesses raised prices to cover tariff costs and now could owe or intend to provide refunds to customers. The tax rules governing when the refund income is recognized and when the related customer rebate is deductible may not align in the same tax period and thus could create a mismatch in timing. The characterization and timing of any customer refunds or rebates raises additional accounting method questions in terms of when that liability is fixed, when it might be deductible, etc.

What if a tariff refund claim has been bought or sold?

Some businesses have "sold" the right to tariff refunds to third parties. These transactions raise their own set of tax questions around whether, when, and how to calculate, characterize, and recognize any resulting gain or loss. For example, does the seller recognize capital gain or ordinary income on the disposition of a refund claim, and how does the buyer determine its cost basis in the acquired claim?

What if an affiliate paid the tariffs but the refund is received by a different entity?

In many multinational structures, transfer pricing arrangements could have been modified such that a non-US entity in the group may have borne the tariff cost even though the US entity (importer of record) is the party that paid the tariff and is entitled to the refund. This mismatch raises transfer pricing and international tax questions — including potential implications under the base erosion and anti-abuse tax (BEAT).

Method changes needed to account for R&E expenditures

With the restoration of immediate expensing for domestic research or experimental (R&E) expenditures under new Section 174A of the OBBBA, all taxpayers with domestic R&E costs will need to file a statement in lieu of Form 3115 for the 2025 tax year — regardless of whether they elect to deduct or capitalize those expenditures, to comply with new Section 174A.

Rev. Proc. 2025-28 addresses two separate method changes — one to adopt the new Section 174A framework for 2025 and beyond, and another to accelerate unamortized domestic R&E costs capitalized during the 2022–2024 period — both of which may be reported on a single statement.

The new rules introduce a number of complexities and planning considerations that taxpayers should evaluate early, including:

- Optionality to deduct or capitalize and amortize domestic R&E expenditures. Taxpayers can immediately expense domestic R&E expenditures paid or incurred during the tax year under Section 174A(a) or capitalize and amortize under Section 174A(c). However, unlike the project-by-project flexibility under pre-TCJA Section 174, Section 6 of Rev. Proc. 2025-28 appears to indicate an "all-or-nothing approach" as it relates to the election to capitalize and amortize domestic R&E

expenditures under Section 174A(c) — taxpayers must capitalize all qualifying domestic R&E expenditures or none at all. Further, for taxpayers that adopt the Section 174A(c) method, the 60-month amortization period for those expenditures does not begin until the beginning of the month in which the taxpayer first realizes benefits from the expenditures, which may delay the start of cost recovery relative to the prior regime. Finally, it is unclear whether changing to Section 174A(c) capitalization and amortization is an annual election or a method of accounting. Further guidance, though not immediately expected, is anticipated to provide clarity on these points.

- Section 59(e) election. As an alternative to immediate expensing or capitalization under Section 174A(c), taxpayers may elect 10-year amortization under Section 59(e)(2)(B). This is an annual election to capitalize a specified dollar amount that does not require a formal method change — a taxpayer first adopts the deduction method under Section 174A(a) and then attaches a statement to its timely filed return to elect Section 59(e) treatment for that year. Importantly, this election is made at the partner level and cannot be made by partnerships themselves. Further, the amortization period starts in the month in which the expenditures were paid or incurred.

- Section 163(j) interaction. Domestic R&E expenditures are only an addback to adjusted taxable income (ATI) for purposes of the Section 163(j) business interest limitation if they are capitalized and amortized under either Section 174A(a) with a Section 59(e) election or pursuant to an election under Section 174A(c). That is, amounts that are deducted currently under Section 174A(a) are not permitted to be added back to determine ATI, even if they are capitalized for financial reporting purposes. For taxpayers that are at or near their Section 163(j) limit, it is important to model this interaction, as elective capitalization may enhance ATI and interest deductibility in tax year beginning in or after 2025, while also coordinating with projected Section 163(j) positions, other elections, and collateral items such as Section 170 limits and other taxable-income-based provisions.

- State conformity. States that do not conform to the OBBBA provisions will continue to require the same state-level R&E adjustments that taxpayers have been computing for the past several years, regardless of the federal treatment elected. Companies should not assume that a change in federal method eliminates the need for separate state analyses, particularly in states with fixed-date conformity or selective decoupling from federal R&E provisions.

- Entity-level optionality. While in general there is no flexibility to split the treatment of costs within a single entity, different legal entities within a group are not required to adopt the same approach. Each legal entity may elect different treatment for its 2025 costs and recovery of its pre-2025 capitalized amounts. There is some ambiguity as to the level at which this decision is made — the IRS has described it both as an "election" (suggesting the taxpayer level or at the trade or business level) and as a "method change" (that could apply at the trade or business level). There is no published guidance resolving this question at this time. Additionally, there is no requirement to be consistent between pre-2025 and 2025 costs, meaning an entity could accelerate all pre-2025 capitalized amounts while electing to capitalize its 2025 expenditures, or vice versa.

Given the number of decisions involved and the compressed timeline for the 2025 filing season, companies should model their Section 174A elections and evaluate downstream effects well in advance of filing. In addition to potential exposure to CAMT or BEAT and other impacts already discussed, companies also should consider cost classification, intercompany arrangements, and location of R&E activities as they relate to the longer 15-year amortization requirement applicable to foreign R&E expenditures.

For more information on these changes, please see our PwC Tax Insights: Section 174A restores optionality to tax treatment of US research activities, and IRS provides a clear path on new options for domestic R&E expenditures.

Joint Committee on Taxation's (JCT) explanation elaborates on some OBBBA provisions

The recently published OBBBA Blue Book, which provides an explanation of tax legislation passed by the most recent Congress and signed into law and the estimated budget effects of this tax legislation, largely restates and describes the statutory provisions as enacted, adding useful context in several areas by confirming interpretive positions that are summarized below.

- Section 163(j) interest capitalization ordering. The Blue Book provides a detailed ordering rule: Section 163(j) applies after Sections 263(g) and 263A(f) but before any other provision under which interest is mandatorily or electively capitalized. It clarifies that the amount allowed under Section 163(j)(1) is applied first to capitalizable business interest, then to deductible business interest, and that no carryforward portion is treated as interest to which a capitalization provision applies. The Blue Book includes an illustrative example that provides practical guidance not readily apparent from the statutory text alone.
- Qualified production property. The Blue Book discusses the definition of "qualified production activity" as manufacturing, production, or refining of tangible personal property resulting in a "substantial transformation." It identifies excluded uses (offices, administrative services, lodging, parking, sales, research, and software development/engineering) and discusses the special rule for previously unused property and the 10-year recapture period.
- Sections 174/174A transition mechanics. The Blue Book confirms a Section 481(a) cutoff basis for the transition to the new R&E expensing regime (no catch-up adjustment), identifies the small business retroactive election deadline of July 6, 2026, and addresses Section 280C regarding research credit coordination where the Section 41 credit exceeds the Section 174 deduction for the year. Section 481 is discussed exclusively in the context of Sections 174/174A. The default rule, as described by the Blue Book, states the change is made on a cutoff basis with no Section 481(a) catch-up adjustment, applying only to expenditures paid or incurred in tax years beginning after December 31, 2024. Descriptions also are provided on the "small business" and "accelerated amortization" elections.
- Section 168(k) bonus depreciation. The Blue Book tracks the statutory language closely, confirming the mechanical operation of the acquisition-date trigger and the election to retain the 40% allowance for the first tax year ending after January 19, 2025.
- Section 170 corporate charitable contributions. The Blue Book provides an overview of the new 1% limitation and historical 10% limitation for corporate charitable contributions and provides that "the provision allows a corporate taxpayer to deduct a charitable contribution only to the extent that the aggregate amount of the charitable contributions exceeds one percent of the taxpayer's taxable income (the ''one-percent floor'') and does not exceed 10 percent of the taxpayer's taxable income (the ''10-percent limit''); therefore, in a taxable year, a taxpayer may only deduct total charitable contributions of up to nine percent of a taxpayer's taxable income." The JCT then notes that a technical correction may be needed for the statute to reflect the intent of the rule.

Recapping domestic guidance issued in response to OBBBA

A year after extensive changes were made by OBBBA, Treasury and the IRS have issued a flurry of guidance consisting of notices, revenue procedures, and proposed regulations. The following summarizes the key guidance issued to date:

Section 168(k) bonus depreciation • Preliminary guidance on bonus depreciation provides familiar rules and favorable elections	Notice 2026-11 provides updated rules on bonus depreciation, including favorable elections and transition relief for taxpayers placing property in service after January 19, 2025.
Section 168(n) qualified production property • Notice 2026-16 provides framework for new 100% depreciation election.	Notice 2026-16 introduces an interim framework for the new 100% depreciation election for qualified production property placed in service after July 4, 2025, including guidance on the "substantial transformation" standard and excluded uses.
Sections 55, 56A, and 59 corporate alternative minimum tax (CAMT) • Interim rules deliver comprehensive relief for companies subject to the CAMT	Notice 2026-7 expands administrative guidance on CAMT and computing adjusted financial statement income.
Section 174A domestic R&E expenditures • IRS provides a clear path on new options for domestic R&E expenditures	Rev. Proc. 2025-28 outlines procedures for adopting the new Section 174A framework and accelerating unamortized domestic R&E costs from the 2022–2024 period, including highlighting state nonconformity considerations.
Section 45Z clean fuel production credit • Proposed rules provide clarity for clean fuel credits	Proposed regulations include a framework for the clean fuel production credit, providing initial clarity on eligibility and computation rules.
June 2026 45ZCF-GREET model • Department of Energy (DOE) provides clarity with updated guidelines and 45CF-GREET model	Guidelines and updates to the 45ZCF-GREET model for calculating lifecycle greenhouse gas (GHG) emissions under Section 45Z.
Section 7701(a)(52) material assistance from a prohibited foreign entity • Interim guidance on prohibited foreign entity restrictions provides clarity while raising questions	Notice 2026-15 provides guidance on "material assistance" restrictions relevant to credit eligibility under the foreign entity of concern rules.

Companies should continue to monitor developments, consider protective positions where guidance is incomplete, and evaluate whether available elections, fact changes, or accounting method changes could help manage taxable income, cash tax position, effective tax rate, and other tax attributes.

Let’s talk

For a deeper discussion of how these developments might affect your business, please contact one of the PwC professionals listed below:

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