Current Status of Issue

- Tier I status as of 1/22/10

Executing IMT Strategy for Tier I Issues

Audit Teams Should:

- ❑ Establish the Tier I Issue on IMS using the UIL code per the ID Directive.
- ❑ Research the issue on the Tier I website.
- ❑ Communicate with the IMT early to determine the strategy and any special requirements for the issue.
- ❑ Consider the issue in the audit planning and risk assessment in accordance with the IMT strategy.
- ❑ Utilize the audit tools and techniques provided by the IMT to develop the issue.
- ❑ Resolve the issue using all resolution tools in alignment with the IMT strategy.

Issue Management Team (IMT)

Issue Executive Owner - Sergio Arellano

Issue Champion - Jolanta Sander

Senior Managers to Technical Advisors – Paula Farmer and Greg Zielinski

Area Counsel – Jim Lanning

Counsel Support— Scott Dinwiddie, Merrill Feldstein, Kirk Chaberski, Ben McClendon

Appeals— Vallery Henry

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Tier 1

IRS LARGE BUSINESS AND INTERNATIONAL DIVISION

Tier I

Repairs vs. Capitalization Change in Accounting Method—CAM

Quick Reference Guide

November, 2010

Issue Owner Executive (IOE)

Sergio Arellano, Industry Director,

Retailers, Food, Pharmaceutical and Healthcare

Tier I: Repairs vs. Capitalization Change of Accounting Method

Issue Description

Taxpayers are filing Forms 3115 requesting a Change in Method of Accounting (CAM) for assets. These requests seek to re-characterize costs previously capitalized under §263(a) as repairs currently deductible under §162. These CAMs involve substantial §481(a) adjustments for assets previously placed in service.

The determination as to whether an expenditure qualifies as a currently deductible repair, or is required to be capitalized is a factual determination. Sufficient contemporaneous records and/or oral testimony are required to justify a change for expenditures the taxpayer has previously capitalized for books and for tax.

This is a cross industry issue. The Issue Management Team will establish a consistent approach both within and between industries to resolve these issues.

Issues include:

1. Real Property Issues;
2. Network Asset Issues; and
3. Store Remodel Issues

Administrative Codes

UIL Codes:

263.14-01

ITAC 1400

Industry Director Directives (IDDs)

Industry Director Directive # 1 issued on 1/22/10- elevates the issue to Tier I status.

http://www.irs.gov/businesses/article/0,,id=218608,00.html

Industry Director Directive # 2 issued on 1/22/10- Change of Accounting Method, Advance Consent and Automatic Procedures

http://www.irs.gov/businesses/article/0,,id=218610,00.html

Mandatory IDRs

The IDR below is not mandatory:

http://www.irs.gov/businesses/article/0,,id=231755,00.html

Appeals Settlement Guidelines (ASGs)

Currently there are no ASGs for this Tier I issue.

Issue Specialization Team (IST)

There is no IST for this issue.

Administrative & Technical Guidance

Internal Revenue Code Section §263(a)
US CODE: Title 26 263(a) Capital Expenditures

Internal Revenue Code Section §263A(g)(1)
US CODE: Title 26 263A Capitalization of Self Constructed Property

Treasury Regulations §1.263(a)
Capital Expenditures 26 CFR 1.263(a)-1.pdf
Examples - Cap. Expend. 26 CFR 1.263(a)-2.pdf
Election - deduct or capitalize 26 CFR 1.263(a)-3.pdf

Treasury Regulations §1.162-4
Repairs Regulations 26 CFR 1.162-4.pdf

Treasury Regulations §1.263A-2

Rules for Property Produced by the Taxpayer 26 CFR 1.263A-2.pdf

Revenue Ruling 2001-4 which provides three scenarios with supporting law that demonstrate how the purpose, physical nature and effect of the work performed will result in decidedly different tax treatments.

Revenue Procedure 2009-39 provides automatic consent provisions for Change in Accounting Methods for a taxpayer that wants to change their method of accounting from capitalizing under §263(a) costs paid or incurred to repair and maintain tangible property to treating them as repair expenses under section §162 and 1.162-4.

This Revenue Procedure also applies to taxpayers that want to change their unit of property to determine the deductibility of repairs. Taxpayers must follow specific rules including stipulating to certain criteria and filing a 3rd copy of Form 3115.

Audit Technique Guide was issued November 2010.