

[4830-01-p]

Published July 20, 2004

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

REG-124405-03

RIN 1545-BC13

Optional 10-Year Writeoff of Certain Tax Preferences

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations relating to the optional 10-year writeoff of certain tax preference items under section 59(e) of the Internal Revenue Code (Code). These proposed regulations provide guidance on the time and manner of making an election under section 59(e). The regulations also provide guidance on revoking an election under section 59(e). The regulations reflect changes to the law made by the Tax Reform Act of 1986, the Technical and Miscellaneous Revenue Act of 1988, and the Omnibus Budget Reconciliation Act of 1989.

DATES: Written or electronic comments and requests for a public hearing must be received by October 18, 2004.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-124405-03), room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR

(REG-124405-03), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC or sent electronically via the IRS Internet site at [www.irs.gov/regs](http://www.irs.gov/regs) or via the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov) (IRS and REG-124405-03).

FOR FURTHER INFORMATION CONTACT: Concerning these proposed regulations, Eric B. Lee, (202) 622-3120; concerning submissions of comments and requests for a public hearing, LaNita VanDyke, (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

**Paperwork Reduction Act**

The collection of information contained in this notice of proposed rulemaking has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the **Office of Management and Budget**, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224. Comments on the collection of information should be received by September 20, 2004. Comments are specifically requested concerning:

Whether the proposed collection of information is necessary for the proper performance of the functions of the IRS, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collection of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

The collection of information in this proposed regulation is in §1.59-1(b). This collection of information is required by the IRS to verify compliance with section 59(e). This information will be used to determine whether the amount of tax has been calculated correctly. The collection of information is required to obtain a benefit. The respondents are certain taxpayers who pay or incur expenditures described in section 59(e)(2).

Taxpayers provide the information on a statement that is attached to their federal income tax return for the taxable year the section 59(e) election is effective.

The estimated burden for the collection of information in §1.59-1(b) is as follows:

Estimated total annual reporting burden: 10,000 hours.

Estimated annual burden per respondent: 1 hour.

Estimated number of respondents: 10,000.

Estimated annual frequency of responses: On occasion.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential as required by 26 U.S.C. 6103.

### **Background**

This document contains proposed amendments to 26 CFR part 1 under section 59(e) of the Code. Section 59(e)(1) allows taxpayers to elect to deduct any qualified expenditure ratably over a 10-year period (3-year period in the case of circulation expenditures described in section 173) beginning with the taxable year in which the expenditure was made (or, in the case of a qualified expenditure under section 263(c), over the 60-month period beginning with the month in which such expenditure was paid or incurred). Section 59(e)(2) defines qualified expenditure as any amount which, but for an election under section 59(e), would have been allowed as a deduction (determined without regard to section 291) for the taxable year in which paid or incurred under section 173 (relating to circulation expenditures), section 174 (relating to research and experimental expenditures), section 263(c) (relating to intangible drilling and development expenditures), section 616(a) (relating to development expenditures), or section 617(a) (relating to mining exploration expenditures).

Section 59(e)(4)(A) states that a n election under section 59(e) (section 59(e) election) may be made with respect to any portion of any qualified expenditure. The legislative history of section 59(e) suggests that this allows a section 59(e) election to be made Adollar for dollar.® See H. R. Rep. 99-426, 99th Cong., 1st Sess. 327 (1985), 1986-3 (Vol. 2) C.B. 1, 327; S. Rep. No. 99-313, 99th Cong., 2d Sess. 539 (1986), 1986-3 (Vol. 3) C.B. 1, 539.

Section 59(e)(4)(B) states that a section 59(e) election may only be revoked with the consent of the Secretary.

Provisions similar to those currently contained in section 59(e) were originally enacted as section 58(i) under the Tax Equity and Fiscal Responsibility Act of 1982, (Public Law 97-248; 96 Stat. 324). Under section 58(i)(1), the optional 10-year writeoff was available only to individuals. Section 58(i)(5)(C) directed the Secretary to promulgate regulations governing the time and manner for making an election under section 58(i) (section 58(i) election).

Section 5f.0(a)(2)(i)(A) and (B) of the temporary Income Tax Regulations that were promulgated under section 58(i) required that a section 58(i) election be made by the later of the due date (including extensions) of the income tax return for the taxable year for which the election was to be effective, or April 15, 1983. TD 7870, 48 FR 1486. Section 5f.0(a)(3) provided that a section 58(i) election was made by attaching a statement to the income tax return (or amended return) for the taxable year in which the election was made. Section 5f.0 was redesignated as §301.9100-5T by TD 8435, 57 FR 43893 on October 15, 1992.

Section 59(e) was enacted as part of the Tax Reform Act of 1986 (Public Law 99-514; 100 Stat. 2085) and, unlike section 58(i), is not limited to individuals. While both the Senate Finance Committee Report and the House Ways and Means Committee Report state that the time and manner of the election would be governed by regulations, Congress did not include a provision similar to former section 58(i)(5)(C) directing the Secretary to promulgate regulations governing the time and manner for making a section 59(e) election. See H. R. Rep. No. 99-426, 99th Cong., 1st Sess. 327 (1985), 1986-3 (Vol. 2) C.B. 1, 327; S. Rep. No. 99-313, 99th Cong., 2d Sess. 539 (1986), 1986-3 (Vol. 3) C.B. 1, 539.

### **Explanation of Provisions**

The proposed regulations provide that a section 59(e) election shall only be made on a statement attached to the taxpayer's income tax return (or amended return) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. A taxpayer must make a separate election for each specific activity or project with respect to which qualified expenditures are paid or incurred. The statement must be filed no later than the date prescribed by law for filing the taxpayer's original income tax return (including any extensions of time) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. The statement must contain: (i) the taxpayer's name, address, and taxpayer identification number; (ii) the type and amount, for each activity or project, of qualified expenditures identified in section 59(e)(2) the taxpayer elects to deduct

ratably over the applicable period described in section 59(e)(1); and (iii) a description of each specific activity or project to which the qualified expenditures relate. For example, if a taxpayer makes a section 59(e) election with respect to research and experimental expenditures incurred during the taxable year for three separate projects, the election statement must provide for each research project the amount of qualified expenditures subject to the election and a description of the research project. Additionally, the election must be made in terms of a specific dollar amount of qualified expenditure and cannot be made with reference to a formula.

The proposed regulations also provide that a section 59(e) election may be revoked for any project or activity only with the consent of the Commissioner and that such consent will only be granted in rare and unusual circumstances. A taxpayer must request the Commissioner's consent to revoke a section 59(e) election prior to the end of the taxable year in which the applicable amortization period described in section 59(e)(1) ends. The revocation, if granted, will be effective retroactively to the first taxable year the section 59(e) election was applicable. However, if the period of limitations for the first taxable year the section 59(e) election was applicable has expired, the revocation, if granted, will be effective in the earliest taxable year for which the period of limitations has not expired. For example, if a calendar year taxpayer makes a section 59(e) election for the taxpayer's 2003 taxable year with respect to three different projects and on June 30, 2005, requests consent to revoke the election with respect to one project, the revocation, if granted by the Commissioner prior to the

expiration of the period of limitations for the taxpayer's 2003 taxable year, is effective for the taxpayer's 2003 taxable year. The amount of the qualified expenditures subject to the section 59(e) election with respect to the one project will be deductible in the taxpayer's 2003 taxable year (subject to the requirements of any other provision under the Code, regulations, or any other published guidance) and the taxpayer will be required to amend any income tax returns affected by the revocation.

The proposed regulations apply to a section 59(e) election made for a taxable year ending, or a request to revoke a section 59(e) election submitted, on or after the date the final regulations are published in the **Federal Register**. Additionally, an otherwise valid section 59(e) election filed for a tax year ending prior to the date final regulations are published in the **Federal Register** will not be challenged by the IRS merely because the election was made later than the date prescribed by law for filing the taxpayer's original income tax return (including any extensions of time) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) begins.

### **Special Analyses**

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that the collection of information in these regulations will not have a significant economic impact on a substantial number

of small entities. This certification is based upon the fact that the reporting burden, as discussed earlier in this preamble, is expected to be insignificant. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

### **Comments and Public Hearing**

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and 8 copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department request comments on the clarity of the proposed rules and how the proposed rules can be made easier to understand and comply with. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

### **Drafting Information**

The principal author of these proposed regulations is Eric B. Lee of the Office of Associate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

## List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

## Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

Paragraph 1. The authority citation for part 1 reads, in part, as follows:

Authority: 26 U.S.C. 7805.

Par. 2. Section 1.59-1 is added to read as follows:

### §1.59-1 Optional 10-year writeoff of certain tax preferences.

(a) In general. Section 59(e) allows any qualified expenditure to which an election under section 59(e) applies to be deducted ratably over the 10-year period (3-year period in the case of circulation expenditures described in section 173) beginning with the taxable year in which the expenditure was made (or, in the case of intangible drilling and development costs deductible under section 263(c), over the 60-month period beginning with the month in which the expenditure was paid or incurred).

(b) Election -- (1) Time and manner of election. An election under section 59(e) shall only be made by attaching a statement to the taxpayer's income tax return (or amended return) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) begins. A taxpayer must make a separate election for each specific activity or project with respect to which qualified expenditures are paid or incurred. The statement must be filed no later than the date prescribed by law for filing the taxpayer's original income tax return (including any extensions of time) for the taxable year in which

the amortization of the qualified expenditures subject to the section 59(e) begins. Additionally, the statement must include the following information - -

- (i) The taxpayer's name, address, and taxpayer identification number;
- (ii) The type and amount, for each activity or project, of qualified expenditures identified in section 59(e)(2) the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1); and
- (iii) A description of each specific activity or project to which the qualified expenditures identified in paragraph (b)(1)(ii) of this section relate.

(2) Elected amount. A taxpayer may make an election under section 59(e) with respect to any portion of any qualified expenditure paid or incurred by the taxpayer in the taxable year to which the election applies. An election under section 59(e) must be for a specific dollar amount and the amount subject to an election under section 59(e) may not be made by reference to a formula.

(c) Revocation -- (1) In general. An election under section 59(e) may be revoked for any project or activity only with the consent of the Commissioner. Such consent will only be granted in rare and unusual circumstances. The revocation, if granted, will be effective in the first taxable year in which the section 59(e) election was applicable. However, if the period of limitations for the first taxable year the section 59(e) election was applicable has expired, the revocation, if granted, will be effective in the earliest taxable year for which the period of limitations has not expired.

(2) Time and manner for requesting consent. A taxpayer requesting the Commissioner's consent to revoke a section 59(e) election must submit the

request prior to the end of the taxable year the applicable amortization period described in section 59(e)(1) ends. The application for consent to revoke the election must be submitted to the Internal Revenue Service in the form of a letter ruling request.

(3) Information to be provided. A request to revoke a section 59(e) election must contain all of the information necessary to support why the Commissioner's consent should be granted and must specify the project activity to which the revocation shall apply.

(4) Treatment of unamortized costs. The unamortized balance of the qualified expenditures subject to the revoked section 59(e) election as of the first day of the taxable year the revocation is effective is deductible in the year the revocation is effective (subject to the requirements of any other provision under the Code, regulations, or any other published guidance) and the taxpayer will be required to amend any income tax returns affected by the revocation.

(d) Effective date. These regulations apply to a section 59(e) election made for a taxable year ending, or a request to revoke a section 59(e) election submitted, on or after the date the final regulations are published in the **Federal Register**.

Deputy Commissioner for Services and Enforcement.