

LB&I Process Unit

Knowledge Base – Corporate/Business Issues & Credits

Library Level	Number	Title
Shelf		Accounting Issues
Book	203	Interest Capitalization 263A
Chapter	1	Overview
Section	1	Interest Capitalization Process

Unit Name	Interest Capitalization for Self-Constructed Assets	
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Process Overview

Interest Capitalization for Self-Constructed Assets

NOTE: Under the Tax Cuts and Jobs Act, Public Law 115-97 Act Section 13102, effective for tax years beginning after 12/31/2017, a small business taxpayer is not required to capitalize costs under section 263A. A small business taxpayer is a taxpayer that (a) has average annual gross receipts of \$25 million (indexed for inflation) or less for the 3 prior tax years and (b) is not a tax shelter (as defined in section 448(d)(3)). This Unit is further updated to reflect a change to the ending production period of the aging process of beer, wine, and distilled spirits in Section 263A(f)(4)(B) from December 31, 2019, to December 31, 2020, pursuant to Act Section 144(a) of Public Law 116-94 (H.R. 1865), Further Consolidated Appropriations Act, 2020, This Practice Unit supersedes the March 13, 2019, and the May 29, 2018, Practice Units with the same title.

Many businesses construct assets for use in their operation. For example, a retailer may build stores to sell products made or purchased for resale. A bank may construct a building for a new branch location. A manufacturing company may build a machine for use in the manufacturing process. These businesses may use borrowed funds to construct these assets and their balance sheets may reflect loans, bonds, notes, certificates, or other evidence of indebtedness. Interest paid on this debt may be subject to interest capitalization.

IRC 263A(f) requires interest capitalization if a taxpayer produces property referred to as designated property. If a business constructs designated property and has certain classes of debt, then the business must capitalize, and not expense, the interest. If a taxpayer does not produce designated property, then the interest capitalization rules do not apply.

All real property a taxpayer produces is considered designated property. Designated property also includes produced tangible personal property if the property has:

- A depreciable class life of 20 years or more, or
- An estimated production period exceeding two years, or
- An estimated production period exceeding one year and estimated costs exceeding \$1,000,000.

Process Overview (cont'd)

Interest Capitalization for Self-Constructed Assets

This practice unit identifies taxpayers subject to IRC 263A(f) and covers the steps involved in determining how much interest must be capitalized to the basis of designated property. The method used to determine the amount of interest to capitalize is called the avoided cost method. This practice unit walks the user through steps to assist in determining the information needed to apply the avoided cost method. It assists the user in finding the pieces needed in order to make the computation. It includes a step for a Service-imposed change in accounting method and the calculation of an IRC 481(a) adjustment. It also covers elections a taxpayer may adopt. The unit includes a comprehensive example walking the user through all the steps in computing capitalizable interest.

Detailed Explanation of the Process

Interest Capitalization for Self-Constructed Assets

Analysis

This process unit refers to related parties at various times to alert the user to consider related parties when applying the interest capitalization rules. The Treasury regulations covering interest capitalization refer to related parties when applying certain aspects of the interest capitalization rules. For example, when considering if there is production of designated property, activities and costs of related persons must be considered when applying the designated property requirements.

The regulations also contain anti-abuse rules that refer to related parties. This anti-abuse regulation requires the application of the interest capitalization rules in a manner that is consistent with IRC section 263A(f) and reasonably carries out the purposes of IRC section 263A(f). For example, the regulations indicate the taxpayer may not use certain loans or loan structuring arrangements or other uses of related parties to facilitate the avoidance of interest capitalization. When considering requirements, and making the computations contained in this practice unit, keep in mind the anti-avoidance and related party rules.

Process Applicability

Interest Capitalization for Self-Constructed Assets

If a taxpayer meets the criteria of “producing designated property” and is subject to interest capitalization under IRC 263A(f), then use the steps described in this practice unit to determine the amount of interest required to be capitalized.

Criteria	Resources
<p><u>Producing Designated Property</u></p> <p>The term “produce” includes construct, build, install, manufacture, develop, improve, create, raise, or grow. A taxpayer is treated as producing any property that another party produces for the taxpayer under a contract with the taxpayer or with an intermediary.</p> <p>Designated property includes all real property and three categories of tangible property.</p> <ol style="list-style-type: none"> 1. Property that has a long useful life (depreciable class life of 20 years or more), or 2. Property with an estimated production period exceeding two years, or 3. Property with an estimated production period exceeding one year and estimated costs exceeding \$1,000,000. <p>The thresholds for tangible personal property are applied separately for each unit of property.</p> <p><u>Costs and Activities to Consider</u></p> <p>For purposes of determining whether property is designated property, identify activities and costs arising from the production of the property. Included are all activities and costs if they are performed or incurred by or for the taxpayer or any related person; and all the costs that directly benefit or are incurred to produce the property.</p>	<ul style="list-style-type: none"> ▪ IRC 263A(g) ▪ Treas. Reg. 1.263A-2(a)(1)(i) ▪ Treas. Reg. 1.263A-8(d)(2) ▪ IRC 263A(f) ▪ Treas. Reg. 1.263A-8(b)(1) ▪ Treas. Reg. 1.263A-8(b)(2) ▪ Treas. Reg. 1.263A-10

Process Applicability (cont'd)

Interest Capitalization for Self-Constructed Assets	
Criteria	Resources
<p><u>Exceptions</u></p> <p>The exception to the above rules include:</p> <ol style="list-style-type: none"> 1. Timber and evergreen trees that are more than 6 years old when severed from the roots, or 2. Property a taxpayer produced for use in other than a trade or business or an activity conducted for profit; and 3. Certain property subject to the long-term contract rules of IRC 460. 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-8(b)(3) ▪ Treas. Reg. 1.263A-8(d)(2)(v) ▪ IRC 460
<p><u>De Minimis Exception for Designated Property</u></p> <p>Property that meets de minimis criteria is not designated property. Designated property does not include property with a production period of 90 days or fewer, and the total production expenditures do not exceed \$1,000,000 divided by the number of days in the production period. For example, if the production period is 10 days, then the total production expenditures cannot exceed \$100,000 ($1,000,000 \div 10$).</p> <p>Under the de minimis rule, certain costs should be excluded in determining the total production expenditures. Those costs include the adjusted basis of property used to produce the property; the cost of land, and interest the taxpayer would capitalize to the property if it were designated property.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-8(b)(4) ▪ Treas. Reg. 1.263A-8(b)(4)(ii)

Process Applicability (cont'd)

Interest Capitalization for Self-Constructed Assets	
Criteria	Resources
<p><u>Use of Reasonable Estimates</u></p> <p>The taxpayer determines whether tangible personal property has a one year or two year production period for each separate unit of property. For purposes of applying designated property thresholds to a unit of tangible personal property, the taxpayer must, at the beginning of the production period, reasonably estimate the production period, reasonably estimate the total cost of production for the unit of property, and maintain contemporaneous written records supporting these estimates and classification.</p> <p>If the estimates are reasonable and based on the existing facts at the beginning of the production period, the property's classification does not change in later periods, even if the actual length of the production period or the actual cost of production differs from the estimates.</p> <p>To be considered reasonable, estimates of the production period and the total cost of production must include the anticipated expenses and time for delay, rework, change orders, and technological, design, or other problems. However, the estimates may disregard the basis of assets used to produce the unit of property and any interest that the taxpayer would be required to capitalize if the unit constituted designated property.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-8(b)(2)(iii)

Summary of Process Steps

Interest Capitalization for Self-Constructed Assets

Process Steps

The steps below explain the process to apply the interest capitalization rules under IRC 263A(f).

Step 1	Determine the Unit of Property
Step 2	Determine the Production Period
Step 3	Determine the Computation Period
Step 4	Determine the Measurement Dates

Summary of Process Steps (cont'd)

Interest Capitalization for Self-Constructed Assets

Process Steps

The steps below explain the process to apply the interest capitalization rules under IRC 263A(f).

Step 5	Calculate the Accumulated Production Expenditures
Step 6	Apply the Avoided Cost Method
Step 7	Impose a Change in Accounting Method

Step 1: Determine the Unit of Property

Interest Capitalization for Self-Constructed Assets

Step 1

Determine the unit of property. Each unit of designated property must include all components of the property.

Considerations	Resources
<p><u>Unit of Property</u></p> <p>It is critical to determine the unit of property (real or tangible) because it is the basis for the rest of the interest capitalization process. The computation of accumulated production expenditures (APEs) and the determination of the production period is based on each unit of property.</p> <p><u>Unit of “Real Property”</u></p> <p>Each unit of real property includes components of real property a taxpayer or related person owns that are functionally interdependent (explained on next slide); and an allocable share of any common features (explained on next slide) a taxpayer or related person owns that is real property even though the common feature does not meet the functional interdependence test; and land on which the real property (including any common features) is situated, land subject to setback restrictions for such property, and any other contiguous portion of the tract of land other than land that a taxpayer holds for a purpose unrelated to the unit of property being produced.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-10(b)(1)▪ Treas. Reg. 1.263A-10(b)(6), Examples

Step 1: Determine the Unit of Property (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 1](#)

Considerations	Resources
<p><u>Unit of "Real Property" (cont'd)</u></p> <p>Functional interdependence depends on how the taxpayer will use the real property. If a taxpayer produces real property for its own use or for a related person's use, components are functionally interdependent if the placing in service of one component is dependent on the placing in service of another component by the taxpayer or related person. If a taxpayer produces real property for sale, components are functionally interdependent if the taxpayer customarily sells them together as a single unit.</p> <p><u>Common features</u></p> <p>Real property may include common features. Examples include streets, sidewalks, playgrounds, clubhouses, tennis courts, sewer lines, and cables. These features may or may not be physically attached to the real property produced. It is important to note that common features are not held separately for the production of income.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-10(b)(2)▪ Treas. Reg. 1.263A-10(b)(3)

Step 1: Determine the Unit of Property (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 1](#)

Considerations	Resources
<p><u>Unit of “Tangible Property”</u></p> <p>Each unit of tangible personal property includes all components that are functionally interdependent. Functional interdependence depends on if the taxpayer will use or sell the property. When the property is used, if two or more components must be placed in service at the same time, then they are functionally interdependent.</p> <p>If the property is produced for sale, components are functionally interdependent if they are customarily sold together as a single unit. For example, if an aircraft manufacturer customarily sells a completely assembled aircraft, the unit of property includes all components of the completed aircraft. If the manufacturer also customarily sells aircraft engines separately, the taxpayer treats any engines that it reasonably expects to sell separately as a single unit of property.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-10(b)(3)

Step 2: Determine the Production Period

Interest Capitalization for Self-Constructed Assets

Step 2

Determine the production period. Capitalization of interest is required during the production period of a unit of designated property.

Considerations	Resources
<p>Periodic interest computations are made during the production period of the designated property. The period of time for these interest computations is called the computation period. The computation period is the period during which the avoided cost method is used to compute capitalizable interest. Interest is capitalized during each computation period.</p> <p><u>Real Property Production Period</u></p> <p>For a unit of real property, production begins on the first date the taxpayer performs any physical activity. The activity must be a physical activity; planning and design are not considered to be physical activities. Additionally, incidental repairs are not activities that start a production period. Physical activities undertaken to prepare for constructing or improving real property start the production period. Examples include clearing, grading, or excavating raw land; demolishing a building or gutting a standing building; engaging in the construction of infrastructure, such as roads, sewers, sidewalks, cables, and wiring; undertaking structural, mechanical, or electrical activities to a building or other structures; and engaging in landscaping activities.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-8(d)(1)▪ Treas. Reg. 1.263A-12(c)(2)▪ Treas. Reg. 1.263A-12(e)(1)

Step 2: Determine the Production Period (cont'd)

Interest Capitalization for Self-Constructed Assets

Step 2

Considerations	Resources
<p><u>Tangible Property Production Period</u></p> <p>For a unit of tangible personal property, production begins on the first date in which a taxpayer's accumulated production expenditures, including planning and design expenditures, are at least 5% of the total estimated production expenditures for the unit of property.</p> <p><u>End of Production Period</u></p> <p>The end of the production period depends on how a taxpayer will use the unit of property (whether real property or tangible personal property). If a taxpayer produces the unit of property for self-use, the production period ends on the date the taxpayer places the unit in service and all production activities reasonably expected to be undertaken are completed.</p> <p>If a taxpayer produces the unit of property for sale, the production period ends on the date the taxpayer is ready to hold the unit for sale and all production activities reasonably expected to be undertaken are completed. If another party produces the unit of property for the taxpayer under a contract, the production period ends when the taxpayer places the property in service and all production activities reasonably expected to be undertaken are completed. In the case of property that is customarily aged before a taxpayer sells it (such as tobacco, wine, or whiskey), the production period includes the aging period.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-8(d)(1) ▪ Treas. Reg. 1.263A-12(c)(3) ▪ Treas. Reg. 1.263A-12(d)(1)

Step 2: Determine the Production Period (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 2](#)

Considerations	Resources
<p><u>End of Production Period (cont'd)</u></p> <p>Note that under the Tax Cuts and Jobs Act, Public Law 115-97 Act Section 13801, the production period for interest capitalization will not include the aging period for beer, wine, and distilled spirits and applies to interest costs paid or accrued in calendar years beginning after December 31, 2017, but only if paid or accrued on or before December 31, 2019. In addition, Act Section 144(a) of Public Law 116-94 (H.R. 1865), Further Consolidated Appropriations Act, 2020, changed the ending production period of the aging process of beer, wine, and distilled spirits in Section 263A(f)(4)(B) from December 31, 2019, to December 31, 2020.</p> <p>If the taxpayer has a large project with several different units of property, then the production period will end for each unit as each separate unit of property is completed. The production period does not wait for the entire project to complete. For example, if there are separate apartments in a multi-unit building and each is a separate unit of property, the production period ends for each separate apartment when the taxpayer is ready to sell or place each unit in service. However, in the case of a single unit of property, which merely undergoes separate and distinct stages of production, the production period ends at the same time (when all separate stages of production are completed).</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-12(d)(3) ▪ Treas. Reg. 1.263A-12(d)(4) ▪ Treas. Reg. 1.263A-12(b) ▪ Treas. Reg. 1.263A-8(b)(1)(ii)(B) and (C) ▪ <i>Tax Cuts and Jobs Act</i> ▪ <i>Further Consolidated Appropriations Act, 2020</i>

Step 2: Determine the Production Period (cont'd)

Interest Capitalization for Self-Constructed Assets


[Step 2](#)

Considerations	Resources
<p><u>Production Period and Related Person's Activities</u></p> <p>If a person related to the taxpayer performs activities and incurs costs related to the taxpayer's production of designated property, then the taxpayer considers this time when determining the taxpayer's production period. This is regardless of whether the related person is performing only a service or is producing a subassembly or component that the related person is required to treat as an item of designated property.</p> <p>These activities and costs are also taken into account in determining whether a taxpayer produced tangible personal property that is 1-year or 2-year property under Treas. Reg. 1.263A-8(b)(1)(ii)(B) and (C).</p> <p><u>Cessation Period</u></p> <p>Under certain circumstances, the taxpayer may elect to suspend (or pause) capitalizing interest, if production activities cease for at least 120 consecutive days (called the "cessation period").</p> <p>A special rule applies if the cessation period spans more than one taxable year. A taxpayer may suspend capitalizing additional interest to the unit of property beginning with the first measurement period of the taxable year in which the 120-day period is satisfied. This special rule applies on an annual basis to all units of property that satisfy these requirements.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-12(g)

Step 2: Determine the Production Period (cont'd)

Interest Capitalization for Self-Constructed Assets

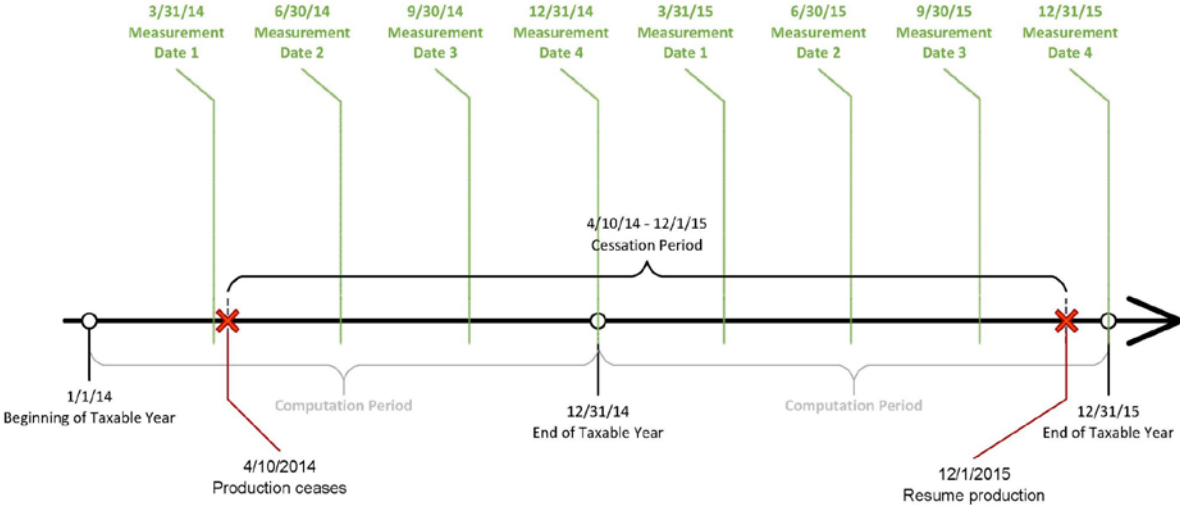
[Step 2](#)

Considerations	Resources
<p><u>Cessation Period (cont'd)</u></p> <p>According to the Treasury regulations, a taxpayer cannot consider activities to have ceased if they cease due to circumstances inherent in the production process, such as normal adverse weather conditions, scheduled plant shutdowns, or delays due to design or construction flaws, the obtaining of a permit or license, or the settlement of ground fill. A taxpayer must resume capitalizing interest to the unit of property beginning with the measurement period during which production activities resume. The suspension of interest is an election made by a taxpayer. The election is a method of accounting that must be consistently applied to all units of property that satisfy the requirements to suspend interest.</p> <p> CAUTION: During a cessation period, a taxpayer may be required to capitalize interest incurred on debt that is traced debt to a unit of property as interest on nontraced debt for the production of other units of property.</p> <p>An example to illustrate this concept can be found in Treas. Reg. 1.263A-9(c)(5)(i)(B).</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(c)(5)(i)(B)

Step 2: Determine the Production Period (cont'd)

Interest Capitalization for Self-Constructed Assets

Step 2

Considerations	Resources
<p data-bbox="209 554 727 586">Illustration of Suspension Period</p> <p data-bbox="209 596 741 629">See Example at Treas. Reg. § 1.263A-12(g)(4)</p>  <p>The diagram illustrates a timeline for interest capitalization. It starts at 1/1/14 (Beginning of Taxable Year). A red 'X' marks the end of production on 4/10/2014. A bracket labeled 'Cessation Period' spans from 4/10/14 to 12/1/15. A red 'X' marks the start of production on 12/1/2015. The timeline includes measurement dates (3/31/14, 6/30/14, 9/30/14, 12/31/14, 3/31/15, 6/30/15, 9/30/15, 12/31/15) and computation periods. The taxable year ends on 12/31/14 and 12/31/15.</p>	<ul style="list-style-type: none"> <li data-bbox="1425 505 1860 572">▪ Treas. Reg. 1.263A-12(g)(4), Example <li data-bbox="1425 582 1852 615">▪ Treas. Reg. 1.263A-12(g)(1)

Step 3: Determine the Computation Period

Interest Capitalization for Self-Constructed Assets

Step 3

Determine the computation period needed to make the avoided cost calculation.

Considerations	Resources
<p><u>Use of the Computation Period</u></p> <p>The avoided cost method is the method used to determine the amount of interest to capitalize to designated property. The computation period is the time-frame used to compute the interest to capitalize. If a taxpayer chooses the taxable year as the computation period, the taxpayer makes a single avoided cost method calculation for each unit of property for the entire taxable year. See Diagram 1 (on slide 23) for an illustration of the taxable year used as the computation period.</p> <p>If a shorter computation period is used, the taxpayer must make separate avoided cost method calculations for each unit of property for each computation period within the taxable year. See Treas. Reg. 1.263A-9(f)(3), Example 2. Computation periods cannot include portions of more than one taxable year. Except in the case of a short taxable year, each computation period within a taxable year must be the same length. In the case of a short taxable year, see Treas. Reg. see Treas. Reg. 1.263A-9(f)(1)(i). The same computation period(s) must be used for all designated property produced during a single taxable year. The choice of a computation period is a method of accounting and a change requires consent of the Commissioner under IRC 446(e).</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(f)(3)▪ Treas. Reg. 1.263A-9(f)(1)(i)▪ IRC 446(e)

Step 4: Determine the Measurement Dates

Interest Capitalization for Self-Constructed Assets

Step 4

Determine the measurement dates used in the determination of capitalized interest.

Considerations	Resources
<p><u>Determine the Measurement Dates</u></p> <p>The avoided cost method calculation requires a minimum number of measurement dates. The measurement dates depend on the length of the computation period. If a taxpayer uses the taxable year as the computation period, then the measurement dates must be at least quarterly, but can be more frequent. See Diagram 2 (on slide 23) for an illustration of quarterly measurement dates.</p> <p>If a taxpayer uses a computation period shorter than the taxable year, then measurement dates must occur at least twice during each computation period and measurement dates must occur at least four times during the taxable year (or consecutive 12 months in the case of a short taxable year).</p> <p>Measurement dates must occur at equal intervals during each computation period, except in the case of a short taxable year. In the case of a short taxable year, the taxpayer may treat a period shorter than the regular computation period as the first or last computation period or as the only computation period if the year is shorter than the regular computation period. The same measurement dates must be used for all designated property produced during the computation period.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(f)(2)(i)

Step 4: Determine the Measurement Dates (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 4](#)

Considerations	Resources
<p><u>Determine the Measurement Dates (cont'd)</u></p> <p>Unlike the computation period, measurement dates are not a method of accounting. A taxpayer may modify the frequency of measurement dates from year to year without requesting consent from the Commissioner.</p> <p><u>Measurement Period</u></p> <p>The measurement period begins on the first day following the preceding measurement date and ends on the measurement date. The measurement periods are needed for the avoided cost computation. For example, if quarterly measurement dates are used, April 1st – June 30th is a measurement period. In other words, April 1 is the first day of the measurement period, and June 30 is both a measurement date and the last day of a measurement period. See Diagram 1 (next slide).</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(f)(2)(ii)▪ Treas. Reg. 1.263A-9(f)(2)(iii)

Step 4: Determine the Measurement Dates (cont'd)

Interest Capitalization for Self-Constructed Assets

Step 4

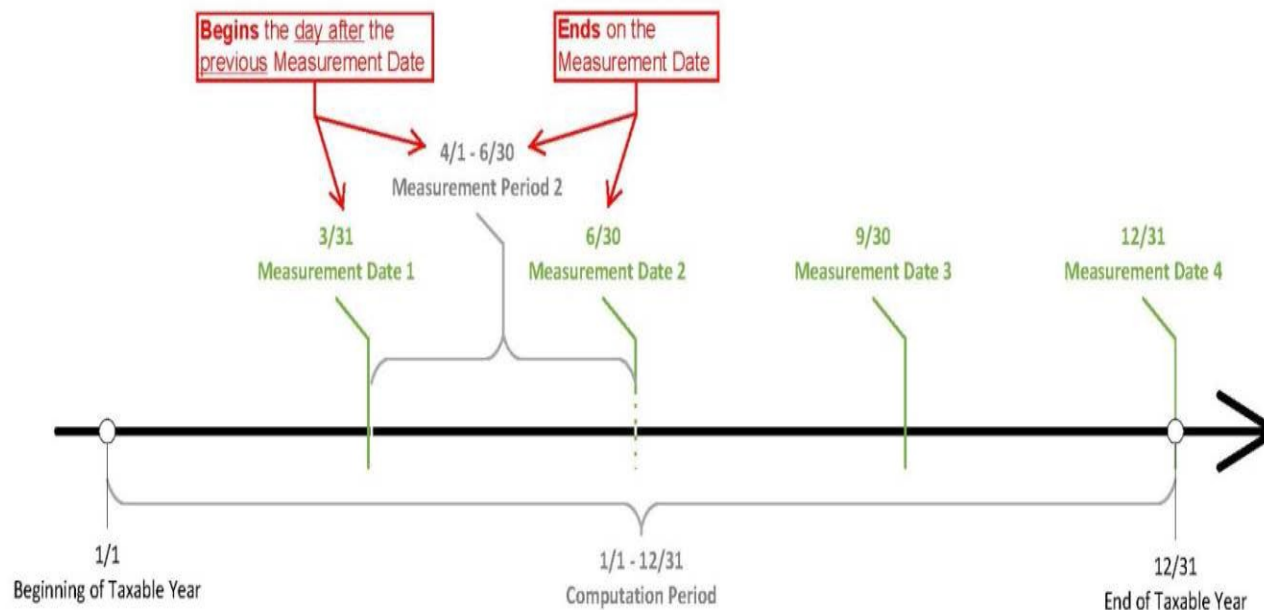
Considerations

Resources

Measurement Period (cont'd)

- [Treas. Reg. 1.263A-9\(f\)\(2\)\(ii\)](#)

Diagram 1: Illustration of the Measurement Period



Step 4: Determine the Measurement Dates (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 4](#)

Considerations	Resources
<p><u>Measurement Period (cont'd)</u></p> <p>The first measurement date on which a taxpayer must take accumulated production expenditures into account for a unit of property is the first measurement date following the beginning of the production period for the unit of property. For example, a taxpayer uses quarterly measurement dates based on a calendar year computation period. The taxpayer begins production on a unit of designated property on 01/13. The first measurement date to consider accumulated production expenditures is 03/31. See Diagram 2 on the next slide.</p> <p>The final measurement date on which a taxpayer must take accumulated production expenditures into account for a unit of property is the first measurement date following the end of the production period for the unit of property. Using the same facts as above, the production ends on 08/06, therefore the final measurement date to consider accumulated production expenditures is 09/30. See Diagram 2 on the next slide. A taxpayer must take accumulated production expenditures into account for a unit of property on all intervening measurement dates. See Diagram 2 on the next slide.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(f)(2)(iii)

Step 4: Determine the Measurement Dates (cont'd)

Interest Capitalization for Self-Constructed Assets

Step 4

Considerations	Resources
<ul style="list-style-type: none"> Diagram 2: Illustration of measurement dates taking accumulated production expenditures into account. Assume quarterly measurement dates are used and the production period for the unit of property begins January 13 and ends August 6. <p>The diagram illustrates the timeline for determining measurement dates. It starts at 1/1 (Beginning of Taxable Year) and ends at 12/31 (End of Taxable Year). A yellow bar highlights the production period from 1/13 to 8/6. Four measurement dates are marked: 3/31 (Measurement Date 1), 6/30 (Measurement Date 2), 9/30 (Measurement Date 3), and 12/31 (Measurement Date 4). Red 'X' marks indicate that the 3/31, 6/30, and 9/30 measurement dates are taken into account, while the 12/31 date is not. A computation period from 1/1 to 12/31 is also shown.</p>	<ul style="list-style-type: none"> Treas. Reg. 1.263A-9(f)(2)(iii)

Step 5: Calculate Accumulated Production Expenditures

Interest Capitalization for Self-Constructed Assets

Step 5


Calculate the accumulated production expenditures related to a unit of property.

Considerations	Resources
<p><u>Accumulated Production Expenditures</u></p> <p>Direct costs and a share of indirect costs are capitalized to each unit of property. These costs are referred as accumulated production expenditures. Included are costs incurred and capitalized to the unit of property prior to the beginning of the production period, including the cost of planning and design activities, the cost of raw land acquired for development, and the cost of a leasehold in mineral properties acquired for development.</p> <p>Also included are costs (other than interest) incurred with respect to the unit of property during each measurement period that includes the production period. It also includes any interest capitalized after prior computation periods. Finally, included is the adjusted basis of certain assets used to produce the unit of property when used during production. For example, a crane used to build large buildings or a heavy equipment used to clear land. See Treas. Reg. 1.263A-11(d)(2) for an example of allocating the adjusted basis of a bulldozer among different projects based on time.</p>	<ul style="list-style-type: none"> ▪ IRC 263A(a) ▪ Treas. Reg. 1.263A-10(b)(1) ▪ Treas. Reg. 1.263A-11(d) ▪ Treas. Reg. 1.263A-11(d)(2)

Step 5: Calculate Accumulated Production Expend. (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 5](#)

Considerations	Resources
<p> CAUTION: A taxpayer may exclude some of the costs noted above from accumulated production expenditures in certain circumstances when a common feature is included in a unit of real property. See Treas. Reg. 1.263A-10(b)(5)(i)-(v) for specific requirements regarding common features.</p> <p><u>When are Costs Considered?</u></p> <p>A taxpayer first considers costs in computing accumulated production expenditures at the time, and to the extent, the taxpayer would otherwise take them into account under the taxpayer's method of accounting. Interest capitalization only applies during the production period. A taxpayer must capitalize all other costs whether incurred before, during, or after the production period.</p> <p>Sometimes a taxpayer engages a related party in the production of the designated property. Only those costs a taxpayer incurs itself are included in the taxpayer's accumulated production expenditures. The related person includes its own capitalized costs in its own accumulated production expenditures for the unit of property in which the parties engage in mutual production activities. However, a taxpayer treats accumulated production expenditures of any unit of property transferred in a nontaxable transaction as accumulated production expenditures the taxpayer incurred.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-10(b)(5)(i)-(v)▪ Treas. Reg. 1.263A-12(a)▪ Treas. Reg. 1.263A-11(g)

Step 6: Apply the Avoided Cost Method

Interest Capitalization for Self-Constructed Assets

Step 6

Calculate the amount of interest to capitalize under IRC 263A(f).

Considerations	Resources
<p><u>Avoided Cost Method</u></p> <p>The avoided cost method must be used to calculate the amount of interest required to be capitalized under IRC 263A(f). If there is no debt, the rules do not apply.</p> <p>The avoided cost method considers all the outstanding debt and then looks at the amount of interest that could be avoided if the funds expended were used to repay the debt instead of using the funds to produce property. It is irrelevant whether the funds used for production would have been used to repay the debt. The avoided cost method assumes a taxpayer would have repaid the debt. The method does not consider the taxpayer's subjective intentions or any restrictions (including legal, regulatory, contractual, or other restrictions) against repayment or use of the debt proceeds.</p> <p>The avoided cost method requires a taxpayer to capitalize interest incurred for two types of debt: (1) traced debt (discussed next) and (2) other debt up to the amount of excess production expenditures.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(a)(1) &(2)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

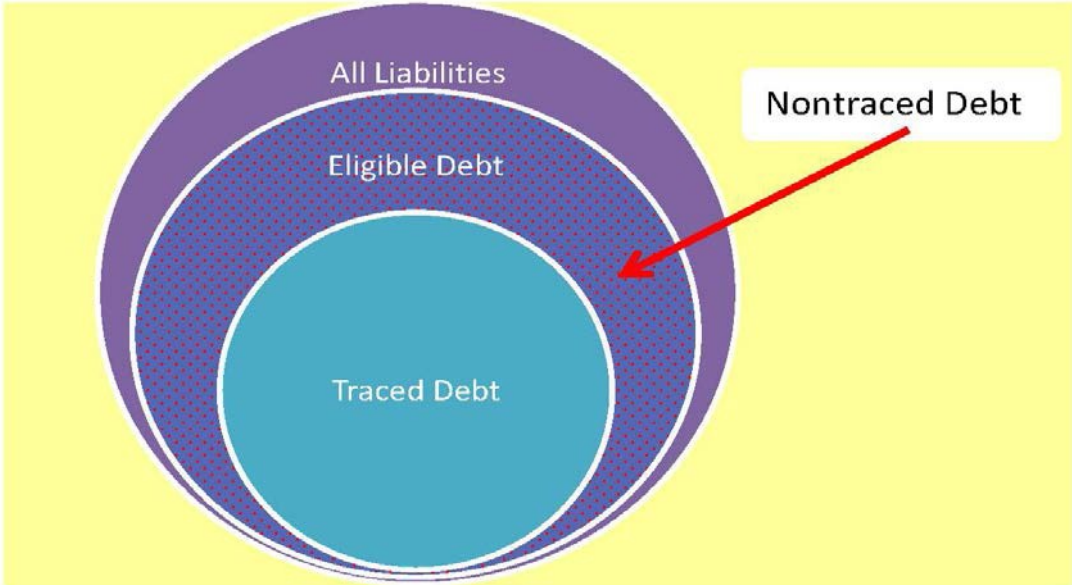
[Step 6](#)

Considerations	Resources
<p><u>Types of Debt</u></p> <p>The avoided cost method requires the capitalization of the traced debt amount and the excess expenditure amount for each unit of property's computation period that includes the production period. The excess expenditure amount is a computation and will be explained in sub-step C. The avoided cost method involves three categories of debt:</p> <ol style="list-style-type: none">1. Eligible debt2. Traced debt3. Nontraced debt <p>Diagram 3 on the next slide illustrates the relationship between the three categories.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<ul style="list-style-type: none">Diagram 3: Relationship Between Eligible Debt, Traced Debt, and Nontraced Debt 	<ul style="list-style-type: none">Treas. Reg. 1.263A-9(a)(4)Treas. Reg. 1.263A-9(b)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p>There are several steps when considering the amount of interest to capitalize. They are broken into sub-steps to guide the computation from start to finish. Sub-step C, contains several computations and it is broken down further into five parts to aid in making the computation. The sub-steps are as follows:</p> <ol style="list-style-type: none">1. Sub-step A: Identify eligible debt2. Sub-step B: Compute the traced debt amount3. Sub-step C: Compute the excess expenditure amount for each unit of property<ol style="list-style-type: none">i. Subpart 1: Calculate the average excess expenditures for each unit of propertyii. Subpart 2: Calculate interest incurred on nontraced debt during the computation periodiii. Subpart 3: Calculate average nontraced debt for the computation periodiv. Subpart 4: Calculate the weighted average interest ratev. Subpart 5: Calculate the excess expenditure amount for each unit of property4. Sub-step D: Compute the total interest available to be capitalized5. Sub-step E: Compare the sum of excess expenditure amounts for all units of property to the total interest available to be capitalized and determine the amount to capitalize <p>Each sub-step and subpart will be discussed next in greater detail.</p>	

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step A: Identify Eligible Debt</u></p> <p>The first sub-step in the avoided cost method is to identify eligible debt. Eligible debt includes all outstanding debt (as evidenced by a contract, bond, debenture, note, certificate, or other evidence of indebtedness).</p> <p><u>Non-Eligible Debt</u></p> <p>Certain categories of debt do not meet the definition of eligible debt. For example, debt that does not bear interest, such as accounts payable and other accrued items. The exception to this is debt related to a specific unit of property being produced (this debt could be “traced-debt” and is discussed next in sub-step B).</p> <p>Other categories of non-eligible debt include:</p> <ul style="list-style-type: none">▪ Direct or indirect related party debt with an interest rate that is less than the federal rate in effect under IRC 1274(d) when issued▪ Reserves▪ Deferred tax liabilities	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(a)(4)▪ IRC 1274(d)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Non-Eligible Debt (cont'd)</u></p> <p>Other categories of non-eligible debt include (cont'd):</p> <ul style="list-style-type: none"> ▪ Items that are not treated as debt for federal income tax purposes (regardless of treatment for financial or other regulatory reporting requirements) ▪ Federal, state, and local income tax liabilities ▪ Deferred tax liabilities under IRC 453A ▪ Hypothetical tax liabilities (e.g., IRC 460(b) the look-back method) ▪ Debt (or the portion thereof) bearing interest that is disallowed under Treas. Reg. 1.163-8T(m)(7)(ii) ▪ Personal interest debt within the meaning of IRC 163(h)(2) ▪ Qualified residence interest within the meaning of IRC 163(h)(3) ▪ Debt incurred by an exempt organization described in IRC 501(a), unless the debt is directly attributed to the organization's related trade or business income (within the meaning of IRC 512) ▪ A purchase money obligation given by the lessor to the lessee (or a party related to the lessee) in a sale and leaseback transaction involving an agreement qualifying as a lease under Treas. Reg. 5c.168(f)(8)-1 through 5c.168(f)(8)-11 	<ul style="list-style-type: none"> ▪ IRC 453A ▪ IRC 460(b) ▪ Treas. Reg. 1.163-8T(m)(7)(ii) ▪ Treas. Reg. 1.263A-9(f)(2)(iii) ▪ Treas. Reg. 5c.168(f)(8)-1 through 5c.168(f)(8)-11 ▪ Treas. Reg. 5c.168(f)(8)-1(e), Example 2

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step B: Compute the Traced Debt Amount</u></p> <p>Traced debt is outstanding eligible debt that is allocated to the accumulated production expenditures for the unit of property being produced. In other words, the proceeds from the debt is used to pay for the expenses of producing the designated property. The traced debt must be identified on each measurement date. See Treas. Reg. 1.263A-9(b)(2) for additional information. Debt is allocated to expenditures based on how the debt is used. (referring to the allocation rules under Treas. Reg. 1.163- 8T). See Diagram 3 (on slide 30) illustrating the relationship between eligible debt, traced debt, and nontraced debt. Also, see comprehensive example, Step 6 (starting on slide 59) illustrating the avoided cost method calculations.</p> <p><u>Traced Debt Capitalization</u></p> <p>A taxpayer must capitalize total interest incurred on traced debt during each measurement period. Treas. Reg. 1.263A-9(b)(3) provides an example of traced debt capitalization: Taxpayer Z, a calendar year taxpayer is engaged in the production of a unit of designated property during 20X5. The taxpayer choses the taxable year as the computation period with quarterly measurement dates. The production starts on 01/14/X5 and ends on 06/16/X5. On 03/31/X5 and 06/30/X5, the taxpayer has a \$1,000,000 loan allocated to the production expenditures of the designated property. During the period 01/01/X5 through 06/30/X5, the taxpayer incurs \$50,000 of interest on the loan. The taxpayer must capitalize the \$50,000 of interest to the designated property.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(b)(2) ▪ Treas. Reg. 1.163A-8T ▪ Treas. Reg. 1.263A-9(b)(3), example

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources								
<p><u>Sub-step B: Compute the Traced Debt Amount (cont'd)</u></p> <p><u>Election to Not Trace Debt</u></p> <p>A taxpayer may elect not to trace debt. Treas. Reg. 1.263A-9(d). If a taxpayer makes this election, the average excess expenditures and weighted average interest rate are determined by treating all eligible debt as nontraced debt. Treas. Reg. 1.263A-9(d)(2) provides the following example: a calendar year corporation is engaged in the production of a single unit of designated property during 20X5. The taxpayer adopts the taxable year as the computation period and quarterly measurement dates. At each measurement (03/31, 06/30, 09/30, and 12/31) the taxpayer has the following outstanding debt:</p> <table border="1" data-bbox="93 949 1404 1178"> <thead> <tr> <th>Type of Outstanding Debt</th> <th>Amount</th> </tr> </thead> <tbody> <tr> <td>Noninterest-bearing accounts payable traced to the designated property</td> <td>\$100,000</td> </tr> <tr> <td>Noninterest-bearing accounts payable not traced</td> <td>\$300,000</td> </tr> <tr> <td>Interest bearing loans that are eligible debt</td> <td>\$900,000</td> </tr> </tbody> </table> <p>The taxpayer elects to not trace debt. For purposes of calculating the weighted average interest rate, eligible debt at each measurement date is \$1,000,000 (\$100,000 + \$900,000).</p>	Type of Outstanding Debt	Amount	Noninterest-bearing accounts payable traced to the designated property	\$100,000	Noninterest-bearing accounts payable not traced	\$300,000	Interest bearing loans that are eligible debt	\$900,000	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(d) ▪ Treas. Reg. 1.263A-9(d)(2), example
Type of Outstanding Debt	Amount								
Noninterest-bearing accounts payable traced to the designated property	\$100,000								
Noninterest-bearing accounts payable not traced	\$300,000								
Interest bearing loans that are eligible debt	\$900,000								

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step B: Compute the Traced Debt Amount (cont'd)</u></p> <p>The election not to trace debt is a method of accounting. It applies to the determination of capitalized interest for all designated property. The election to use or revoke this method requires consent from the Commissioner under IRC 446(e).</p> <p><u>Sub-step C: Compute the Excess Expenditure Amount for Each Unit of Property</u></p> <p>Basic Formula:</p> $\begin{array}{rcccl} \text{Excess} & & \text{Average Excess} & & \text{Weighted} \\ \text{Expenditure} & = & \text{Expenditures for the} & \times & \text{Average} \\ \text{Amount} & & \text{unit of property} & & \text{Interest Rate} \end{array}$	<ul style="list-style-type: none"> ▪ IRC 446(e) ▪ Treas. Reg. 1.263A-9(c) ▪ Treas. Reg. 1.263A-9(b)(5)(ii)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Subpart 1: Calculate the Average Excess Expenditures for Each Unit of Property</u></p> <p>The first step is to find average excess expenditures for the unit of property for the computation period. This is done by subtracting the traced debt from the accumulated production expenditures on each measurement date during the computation period, and then dividing the sum of these amounts by the number of measurement dates during the computation period.</p> <p>Treas. Reg. 1.263A-9(c)(5)(ii)(B) provides an example of how to compute the average excess expenditures. An example: Taxpayer Z, a calendar year taxpayer is engaged in the production of a unit of designated property during 20X5. The taxpayer chooses the taxable year as the computation period with quarterly measurement dates. The production period for the designated property starts on 01/14/X5 and ends on 06/16/X5.</p> <p>On 03/31/X5 and 06/30/X5 the taxpayer has \$1,000,000 of traced debt related to the designated property. As of the first measurement date, the taxpayer had incurred production costs of \$1,400,000. As of the second measurement date, the taxpayer had incurred \$200,000 more, for a cumulative cost of \$1,600,000. Therefore, the accumulated production expenditures exceed the traced debt related to the designated property on 03/31/X5 by \$400,000 and on 06/30/X5 by \$600,000.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(5)(ii)(B)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Subpart 1: Calculate the Average Excess Expenditures for Each Unit of Property (cont'd)</u></p> <p>The average excess expenditures for the property during 20X5 are \$250,000, found as follows: $([\\$400,000 + \\$600,000 + \\$0 + \\$0] \div 4)$. The production ends on 06/15/20X5, therefore the last two measurement periods are zero. The last measurement period, which has production activities, is the measurement period that ends on the 06/30/20X5 measurement date.</p> <p>The computation requires a weighted average interest rate. The formula for the weighted average interest rate for the computation period:</p> $\frac{\text{Interest Incurred on Nontraced Debt During the Computation Period}}{\text{Average Nontraced Debt for the Computation Period}}$	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(5)(ii)(B) ▪ Treas. Reg. 1.263A-9(c)(6), Examples 1 & 2

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step C: Compute the Excess Expenditure Amount for Each Unit of Property (cont'd)</u></p> <p>See Comprehensive Example, Sub-step C. Also see Treas. Reg. 1.263A-9(c)(6), Examples.</p> <p>The components of the computation will be explained after the following elections which can affect this computation.</p> <p><u>Eligible Taxpayer's Election to Use External Interest Rate</u></p> <p>Eligible taxpayers may elect to use an external interest rate instead of computing the weighted average interest rate. See Treas. Reg. 1.263A-9(e) for additional information. A taxpayer is an eligible taxpayer for the taxable year if the average annual gross receipts of the taxpayer for the three previous taxable years do not exceed \$10,000,000 (the \$10,000,000 gross receipts test) and the taxpayer has met the \$10,000,000 gross receipts test for all prior taxable years beginning after December 31, 1994.</p> <p>The principles of IRC 263A(b)(2)(B) and(C) and Treas. Reg. 1.263A-3(b) apply in determining whether a taxpayer is an eligible taxpayer for a taxable year. If elected, the eligible taxpayer must use the highest Applicable Federal Rate (AFR) under IRC 1274(d) in effect during the computation.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(6), Examples 1 & 2 ▪ Treas. Reg. 1.263A-9(c)(5)(D) ▪ Treas. Reg. 1.263A-9(e) ▪ IRC 263A(b)(2)(B) and (C) ▪ Treas. Reg. 1.263A-3(b) ▪ IRC 1274(d)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets


[Step 6](#)

Considerations	Resources
<p><u>Eligible Taxpayer's Election to Use External Interest Rate (cont'd)</u></p> <p>The use of the AFR-plus-3 method is a method of accounting. The eligible taxpayer makes the election to use the AFR-plus-3 method by using the AFR-plus-3 as the taxpayer's weighted average interest rate. Any change to the AFR-plus-3 method by an eligible taxpayer that has never previously used the method does not require Commissioner consent. Subsequent changes to or from the AFR-plus-3 method requires the Commissioner's consent under IRC 446(e). All changes to or from the AFR-plus-3 method are made on a cut-off basis (i.e. an IRC 481(a) adjustment is not allowed).</p> <p><u>Election to Treat Eligible Debt as Outstanding in Certain Circumstances</u></p> <p>A taxpayer may elect to treat eligible debt that it repays within the 15-day period immediately preceding a quarterly measurement date as outstanding on that measurement date, see Treas. Reg. 1.263A-9(g)(7).</p> <p>When computing the denominator for the weighted average interest rate, any nontraced debt repaid during the computation period will be excluded from nontraced debt outstanding for measurement dates after repayment. Nevertheless, the numerator includes all interest incurred on nontraced debt during the computation period. If nontraced debt is repaid close in time to a measurement date, the numerator will include all interest that accrued on the debt during that measurement period, yet the debt will be wholly excluded from the denominator on the measurement date.</p>	<ul style="list-style-type: none">▪ IRC 446(e)▪ Treas. Reg. 1.263A-9(g)(7)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Election to Treat Eligible Debt as Outstanding in Certain Circumstances (cont'd)</u></p> <p>This “mismatch” could inflate the weighted average interest rate. If a taxpayer satisfies the terms for the election, they may continue to include the underlying nontraced debt in the denominator on the first measurement date after repayment. A taxpayer may make this election or discontinue the election for any computation period and it is not a method of accounting.</p> <p> CAUTION: Special rules apply if a taxpayer has no nontraced debt or if it incurs interest at a rate that is contingent. If the taxpayer does not have traced debt then the weighted average interest rate is the highest applicable Federal rate in effect under IRC 1274(d) during the computation period. If interest is incurred at a rate that is contingent at the time the return for the year that includes the computation period is filed, the amount of interest is determined using the higher of the fixed rate of interest (if any) on the underlying debt or the applicable federal rate in effect under section 1274(d) on the date of issuance.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(g)(7) ▪ IRC 1274(d)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Subpart 2: Calculate Interest Incurred on Nontraced Debt During the Computation Period</u></p> <p><u>How to Find Interest Incurred on Nontraced Debt During the Computation Period</u></p> <p>Interest incurred on nontraced debt during the computation period is the total amount of interest incurred during the computation period on all eligible debt minus the amount of interest incurred during the computation period on traced debt. A taxpayer must include all interest incurred on nontraced debt during the computation period in the numerator of the weighted average interest rate, even if the taxpayer repays the underlying nontraced debt during the computation period.</p> <p><u>Subpart 3: Calculate the Average Nontraced Debt for the Computation Period:</u></p> <p><u>How to Find Average Nontraced Debt for the Computation Period:</u></p> $\frac{\text{Amount of Nontraced Debt Outstanding on Each Measurement Date During the Computation Period}}{\text{Number of Measurement Dates During the Computation Period}}$	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(5)(D) ▪ Treas. Reg. 1.263A-9(c)(6), Example ▪ Treas. Reg. 1.263A-9(c)(5) ▪ Treas. Reg. 1.263A-9(c)(5)(iii)(C)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p data-bbox="84 501 1214 536"><u>Sub-step C: Compute the Excess Expenditure Amount for Each Unit of Property</u></p> <p data-bbox="84 579 1384 762">Nontraced debt is all eligible debt on a measurement date other than traced debt for the unit of property on that measurement date. This may include eligible debt that was previously treated as traced debt or that will be treated as traced debt on future measurement dates. Treas. Reg. 1.263A-9(c)(5)(i)(B) provides the following example regarding the treatment of traced debt:</p> <p data-bbox="84 808 1373 953">In 20X5, a taxpayer starts, but does not finish, the construction of two office buildings which are considered separate units of designated property (Property D and Property E). At the beginning of 20X5, the taxpayer borrowed \$2,500,000 to be used exclusively to finance the production expenditures related to Property D.</p> <p data-bbox="84 999 1398 1145">The taxpayer pays the interest, but the entire principal remains outstanding at the end of 20X5. The taxpayer also has a long-term loan with a principal amount of \$2,000,000 outstanding during all of 20X5. The proceeds of this loan were used to finance the production of Property C, completed in 20X4.</p>	<ul data-bbox="1425 501 1912 572" style="list-style-type: none">▪ Treas. Reg. 1.263A-9(c)(5)(i)(B), Example

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step C: Compute the Excess Expenditure Amount for Each Unit of Property (cont'd)</u></p> <p>The portion of the \$2,500,000 loan allocated to the accumulated production expenditures for Property D is treated as traced debt for each measurement date in 20X5. Any excess of the \$2,500,000 loan that is treated as traced debt on each measurement date during 20X5 is treated as nontraced debt for that measurement date, even though the taxpayer expects the entire \$2,500,000 will be treated as traced debt for Property D on subsequent measurement dates as more of the proceeds are used to finance additional production expenditures. In addition, the \$2,000,000 loan is treated as nontraced debt for 20X5, even though it was treated as traced debt with respect to Property C in a prior period.</p>	<ul style="list-style-type: none">▪ Treas. Reg. 1.263A-9(c)(5)(i)(B), Example

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources										
<p><u>Subpart 4: Calculate the Weighted Average Interest Rate</u></p> <p>If the interest incurred on nontraced debt was \$50,000 and the average nontraced debt for the computation period was \$1,000,000 then weighted average interest rate:</p> $\frac{50,000}{1,000,000} = 5\%$ <p><u>Subpart 5: Calculate the Excess Expenditures Amount for Each Unit of Property</u></p> <table border="0" style="width: 100%;"> <tr> <td style="text-align: center;">Excess Expenditure Amount</td> <td style="text-align: center;">=</td> <td style="text-align: center;">Average Excess Expenditures for the unit of property</td> <td style="text-align: center;">X</td> <td style="text-align: center;">Weighted Average Interest Rate</td> </tr> <tr> <td style="text-align: center;">\$12,500</td> <td style="text-align: center;">=</td> <td style="text-align: center;">250,000</td> <td style="text-align: center;">X</td> <td style="text-align: center;">5%</td> </tr> </table>	Excess Expenditure Amount	=	Average Excess Expenditures for the unit of property	X	Weighted Average Interest Rate	\$12,500	=	250,000	X	5%	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(5)(iii) ▪ Treas. Reg. 1.263A-9(c) ▪ Treas. Reg. 1.263A-9(c)(3), Example
Excess Expenditure Amount	=	Average Excess Expenditures for the unit of property	X	Weighted Average Interest Rate							
\$12,500	=	250,000	X	5%							

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step D: Calculate the Total Interest Available to Be Capitalized</u></p> <p>A taxpayer must compute the total interest available to be capitalized by adding certain interest incurred during the computation period. Included is interest on nontraced debt, plus interest on debt that is borrowed directly or indirectly from a person related to the taxpayer that bears a rate of interest that is less than the federal rate in effect under IRC 1274(d) on the date of issuance. Plus, in the case of a partnership, guaranteed payments for the use of capital (within the meaning of IRC 707(c)), that would be deductible by the partnership if IRC 263A(f) did not apply.</p>	<ul style="list-style-type: none">▪ IRC 1274(d)▪ IRC 707(c)▪ Treas. Reg. 1.263A-9(c)(2)

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p><u>Sub-step E: Compare the Sum of the Excess Expenditure Amounts for All Units of Property to the Total Interest Available to Be Capitalized</u></p> <p>Treas. Reg. 1.263A-9(c)(3) provides the following example: A partnership is owned equally by Corporation A and Individual B and is engaged in the construction of an office building during 20X5. The average excess expenditures for the office building for 20X5 are \$2,000,000. A and B agreed when the partnership was formed that A would be entitled to a guaranteed payment of \$70,000 in exchange for A's capital contribution. The only loan outstanding is from an unrelated lender for \$1,000,000.</p> <p>The loan is nontraced debt and has an annual interest rate of 10 percent. The weighted average interest rate is therefore 10 percent and interest for 20X5 is \$100,000. The excess expenditure amount is \$200,000 (\$2,000,000 x 10%). The interest capitalized is \$170,000 (\$100,000 of interest plus \$70,000 of guaranteed payments).</p> <p>If the total interest available to be capitalized exceeds the sum of the excess expenditure amounts for all units of property, a taxpayer must capitalize each unit of property's excess expenditure amount to that unit. If the sum of the excess expenditure amounts for all units of property exceeds the total interest available to be capitalized, a taxpayer must capitalize only a prorated amount of such interest to each unit of property.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(3) ▪ Treas. Reg. 1.263A-9(c)(7)(i) ▪ Treas. Reg. 1.263A-9(c)(7)(ii) ▪ Treas. Reg. 1.263A-9(c)(7)(iii) ▪ Notice 88-99

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets


[Step 6](#)

Considerations	Resources
<p><u>Sub-step E: Compare the Sum of the Excess Expenditure Amounts for All Units of Property to the Total Interest Available to Be Capitalized (cont'd)</u></p> <p>The amount of interest a taxpayer must allocate to each unit of property equals:</p> $\begin{array}{r} \text{Total Interest Available} \\ \text{To be Capitalized} \end{array} \quad \times \quad \frac{\text{Average Excess Expenditures} \\ \text{for the Unit of Property}}{\text{Sum of Average Excess Expenditures} \\ \text{for all Units of Property}}$	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-9(c)(7)(ii) ▪ Treas. Reg. 1.263A-9(c)(7)(iii) ▪ Notice 88-99

Step 6: Apply the Avoided Cost Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 6](#)

Considerations	Resources
<p data-bbox="84 505 1404 576"><u>Sub-step E: Compare the Sum of the Excess Expenditure Amounts for All Units of Property to the Total Interest Available to Be Capitalized (cont'd)</u></p> <p data-bbox="84 658 1390 915"> CAUTION: In this case, related persons may be required to capitalize interest as well. The sum of the excess expenditures exceeds interest available; therefore, the related person must take the excess expenditures into account when computing capitalized interest for each unit of property. In addition, if the taxpayer is a corporation related to another person for the purposes of the applicable related party rules, then the Service may require in this instance that the deferred interest be excluded from the total interest available for capitalization.</p>	

Step 7: Impose a Change in Accounting Method

Interest Capitalization for Self-Constructed Assets

Step 7

Impose a change in accounting method and compute the required IRC 481(a) adjustment.

Considerations	Resources
<p><u>Accounting Method</u></p> <p>Neither the Code nor the Regulations define the term “method of accounting.” In general, an accounting method is a set of rules under which a taxpayer ascertains when to recognize income and expenses to determine taxable income.</p> <p>The term “method of accounting” includes not only a taxpayer’s overall method of accounting, but also the accounting treatment of any material item. An overall method is a general method of accounting, such as the cash method or the accrual method. A material item refers to any specific item that involves the proper time to include income or deduct expenses. A method of accounting must involve timing. If an accounting practice for an item does not permanently affect the taxpayer’s lifetime taxable income, but does or could change the year in which taxable income is reported (or in which deductions are claimed), the accounting practice for the item involves timing and is therefore considered a method of accounting. A method of accounting that complies with the tax rules and regulations is a permissible method of accounting (i.e., clearly reflects income). An impermissible method of accounting does not comply with the tax rules and regulations. A taxpayer adopts a method of accounting by a consistent pattern of treatment.</p>	<ul style="list-style-type: none"> ▪ IRC 446 ▪ Treas. Reg. 1.446-1 ▪ Rev. Proc. 2002-18 ▪ Issue Snapshot - <i>Basic Method of Accounting Concepts</i>

Step 7: Impose a Change in Accounting Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 7](#)

Considerations	Resources
<p><u>Accounting Method (cont'd)</u></p> <p>A taxpayer adopts a permissible method of accounting by using it on the first return that reflects the overall method or material item. A taxpayer adopts an impermissible method of accounting by using it on two or more consecutively filed returns. Once a taxpayer adopts a method of accounting, a taxpayer cannot change the method, even an impermissible one, without the Commissioner's consent. Capitalization of interest, under IRC 263A, represents a method of accounting. See Treas. Reg. 1.263A-8(a)(3).</p> <p><u>Change in Accounting Method</u></p> <p>A change in treatment of interest from deductible to capitalizable or vice versa is a change in accounting method. When the Service determines a taxpayer's method of accounting for its interest deduction does not clearly reflect income (i.e., the method is impermissible), the Service can change the taxpayer's method to a permissible method (i.e., capitalization under IRC 263A(f)). This is a Service-imposed or involuntary method change. The Service generally makes the change in accounting method in the earliest year under examination. The new method is effective as of the beginning of the year of change.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.263A-8(a)(3) ▪ IRC 263A(f) ▪ Issue Snapshot - <i>Involuntary (Service-Initiated) Method Change</i>

Step 7: Impose a Change in Accounting Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 7](#)

Considerations	Resources
<p><u>Change in Accounting Method (cont'd)</u></p> <p>If the taxpayer used the impermissible method in prior years, the Service will impose the change in accounting method with an IRC 481(a) adjustment and a current year adjustment for each year under examination. The IRC 481(a) adjustment is required to prevent any omissions or duplications of income and expenses that may result from using a method of accounting different from the method of accounting used in prior years.</p> <p>The IRC 481(a) adjustment amount is equal to the cumulative difference between income or expenses recognized under the taxpayer's prior impermissible method and the new permissible method. Calculation of the IRC 481(a) adjustment for interest capitalization requires the examiner to determine the cumulative interest amount that the taxpayer would have capitalized for the production period in prior years under the new method as of the beginning of the year of change. This will require the examiner to request the pertinent information from the taxpayer to calculate the prior year's interest capitalization. The difference between this amount and the amount the taxpayer capitalized under the old method for the production period in prior years represents the IRC 481(a) adjustment. The IRC 481(a) adjustment, whether positive or negative, is taken into account entirely in the year of change (i.e., there is no spread) for a Service-imposed method change.</p>	<ul style="list-style-type: none"> ▪ IRC 481(a) ▪ Issue Snapshot - <i>IRC 481(a)</i> ▪ Issue Snapshot - <i>IRC 481(b) Tax Limitation</i>

Step 7: Impose a Change in Accounting Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 7](#)

Considerations	Resources
<p><u>Change in Accounting Method (cont'd)</u></p> <p>IRC 481(b) provides for a limitation on the tax that results from including the IRC 481(a) adjustment in income entirely in one year. Please see IRC 481(b) Tax Limitation Issue Snapshot to determine if the IRC 481(b) tax limitation is applicable</p> <p>If this is the first year the taxpayer used the impermissible method, the Service will change the taxpayer's method of accounting for the first year under examination in which it used the impermissible method, but the IRC 481(a) adjustment will be zero. Rev. Proc. 2002-18 provides the general procedures for Service-imposed changes in accounting methods. An examiner changing a taxpayer's method of accounting will provide written notice to the taxpayer. The written notice must include a statement that the accounting method issue is being treated as a change in accounting method, provide a clearly labeled IRC 481(a) adjustment, and a description of the new method of accounting. An examiner can adapt the pro forma Service-Imposed Method Change Issue Notice of Proposed Adjustment.</p>	<ul style="list-style-type: none"> ▪ IRC 481(a) ▪ IRC 481(b) ▪ Rev. Proc. 2002-18 ▪ Pro Forma - Service-Imposed Method Change Notice of Proposed Adjustment ▪ Rev. Proc. 2015-13

Step 7: Impose a Change in Accounting Method (cont'd)

Interest Capitalization for Self-Constructed Assets

[Step 7](#)

Considerations	Resources
<p><u>Unauthorized Change in Accounting Method</u></p> <p>As provided previously, once a taxpayer adopts a method of accounting, consent is required to change a method of accounting. A taxpayer requests consent by following the general method change procedures (currently Rev. Proc. 2015-13) and files a Form 3115, Application for Change in Accounting Method.</p> <p>If a taxpayer has adopted a method of accounting for its interest under IRC 263A, and has changed its method of accounting without obtaining consent, the taxpayer has made an unauthorized change in accounting method. This would include a change to the computation period, to or from tracing to not tracing debt, or to or from the weighted average interest rate to or from the AFR-plus-3 interest rate.</p> <p>If a taxpayer has made an unauthorized change in method, an examiner may make any adjustments that are necessary to bring the change in accounting method into compliance (including any IRC 481(a) adjustment), deny the change in accounting method, and place the taxpayer back on its prior method, or deny the change in accounting method and place the taxpayer on any permissible method of accounting. An examiner can adapt the Pro Forma Unauthorized Method Change Issue Notice of Proposed Adjustment.</p>	<ul style="list-style-type: none"> ▪ IRC 263A ▪ IRC 481(a) ▪ Pro Forma - Unauthorized Method Change Issue Notice of Proposed Adjustment

Definitions

Interest Capitalization for Self-Constructed Assets

Description

- Accumulated production expenditures – the cumulative amount of direct and indirect costs that a taxpayer is required to capitalize to a unit of property under IRC 263A(f). See [Step 5](#) for further explanation.
- Avoided cost method – the method a taxpayer uses to compute the amount of interest to capitalize under IRC 263A(f). See [Step 6](#) for additional information.
- Computation period – the avoided cost method computes interest capitalization for each computation period (generally, the taxable year). See [Step 3](#) for further information.
- Designated property – all real property, or tangible personal property satisfying specific requirements that the taxpayer produced. A full discussion is found in [Step 1](#).
- Eligible debt – all of a taxpayer’s outstanding debt, except certain categories of debt. See [Step 6](#) for a full discussion and explanation.
- Measurement date – the avoided cost method computes interest capitalization based on “snapshots” of a taxpayer’s accumulated production expenditures, traced debt, and nontraced debt at various times throughout the computation period. The taxpayer takes these “snapshots” on the measurement dates. See [Step 4](#) for additional discussion.
- Measurement period – begins on the first day following the preceding measurement date and ends on the measurement date (e.g., if quarterly measurement dates are used, April 1 – June 30 is a measurement period). See [Step 4](#) for additional discussion.
- Nontraced debt – Eligible debt not treated as traced debt. See [Step 6](#) for further discussion.
- Traced debt – Eligible debt allocable under the rules of Treas. Reg. 1.163-8T to the accumulated production expenditures of a unit of property on one or more measurement dates. See [Step 6](#) for further discussion.
- Unit of property – used as a basis to determine the accumulated production expenditures of the designated property and to determine the beginning and ending of the production period. See [Step 1](#) for additional information.

Examples of the Process

Interest Capitalization for Self-Constructed Assets

Description

Based on Treas. Reg. 1.263A-9(f)(3), Example 3

Key Facts:

1. Corporation X is a calendar year taxpayer.
2. Corporation X engaged in the production of two units of designated property during 2015.
Unit A: production started on 06/01/2014 and ended on 6/20/2015
Unit B: production started on 4/15/2015, but does not end until 07/31/2016
3. Corporation X adopted the taxable year as its computation period and did not elect not to trace debt.
4. Corporation X uses quarterly measurement dates and pays all interest on Eligible Debt in the quarter incurred.
5. During 2015, Corporation X had two items of Eligible Debt. The debt and the manner in which it is used are as follows:

Loan #	Principal	Annual Rate (Percent)	Period Outstanding	Use of Proceeds
1	\$ 1,000,000	9%	01/01/2015-09/01/2015	Unit A
2	\$ 2,000,000	11%	06/01/2015-12/31/2015	Nontraced

Accumulated production expenditures at the end of each quarter during 2015 are as follows:

Measurement Date	Unit A	Unit B
03/31/2015	\$ 1,200,000	\$ 0
06/30/2015	\$ 1,800,000	\$ 500,000
09/30/2015	\$ 0	\$ 1,000,000
12/31/2015	\$ 0	\$ 1,600,000

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Assume for this example that the taxpayer produced designated property. The property met the designated property requirements and therefore is subject to interest capitalization.

Step 1: Determine the Unit of Property

Assume for this example that Unit A and Unit B are separate units of property for interest capitalization.

Step 2: Determine the Production Period

Unit A: production period began on 06/01/2014 and ended on 6/20/2015

Unit B: production period began on 4/15/2015, and did not end until 07/31/2016

Step 3: Determine the Computation Period

Corporation X adopted the taxable year as the computation period.
Therefore, the computation period begins on 01/01 and ends 12/31.

Step 4: Determine the Measurement Dates

Corporation X uses quarterly measurement dates.
Therefore, the measurement dates are 3/31, 6/30, 9/30, and 12/31.

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 5: Determine the Accumulated Production Expenditures

Measurement Date	Unit A	Unit B
03/31/2015	\$ 1,200,000	\$ 0
06/30/2015	\$ 1,800,000	\$ 500,000
09/30/2015	\$ 0	\$ 1,000,000
12/31/2015	\$ 0	\$ 1,600,000

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 6: Apply the Avoided Cost Method

Sub-step A: Identify eligible debt

Loan #1 and Loan #2 do not meet any of the exceptions in Treas. Reg. 1.263A-9(a)(4). Therefore, Loan #1 and Loan #2 are both eligible debt.

Loan #	03/31/2015	06/30/2015	09/30/2015	12/31/2015
1	\$ 1,000,000	\$ 1,000,000	\$ 0	\$ 0
2	\$ 0	\$ 2,000,000	\$2,000,000	\$2,000,000
Eligible Debt	\$ 1,000,000	\$ 3,000,000	\$2,000,000	\$2,000,000

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 6: Apply the Avoided Cost Method (cont'd)

Sub-step B: Compute the traced debt amount

Trace the use of the proceeds of Loan #1 and Loan #2

	Measurement dates			
Loan #	03/31/2015	06/30/2015	09/30/2015	12/31/2015
1	Unit A	Unit A	Nontraced	Nontraced
2	Nontraced	Nontraced	Nontraced	Nontraced

On 3/31 and 6/30, the proceeds of Loan #1 are traceable under Treas. Reg. 1.163-8T to Unit A. Therefore, Loan #1 is treated as traced debt to Unit A for the Measurement Periods 1/1 to 3/31 and 4/1 to 6/30, or 6 months.

Loan #	Principal	Annual Rate	Monthly Interest	# Months as Traced Debt	Traced Debt Amount
1	\$ 1,000,000	9%	\$ 7,500	6	\$ 45,000

Based on an annual 9 percent rate of interest, Corporation X incurs \$7,500 of interest each month that Loan #1 is outstanding. The interest incurred on Loan #1 from 1/1 to 6/30 (\$7,500/month x 6 months = \$45,000) must be capitalized to Unit A.

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 6: Apply the Avoided Cost Method (cont'd)

Sub-step C: Compute the excess expenditure amount for each unit of property

Calculate average excess expenditures for Unit A:

Unit A	03/31/2015	06/30/2015	09/30/2015	12/31/2015
APEs	\$ 1,200,000	\$ 1,800,000	\$ 0	\$ 0
Traced Debt	\$ (1,000,000)	\$ (1,00,000)	\$ 0	\$ 0
Excess Exps.	\$ 200,000	\$ 800,000	\$ 0	\$ 0

$$\frac{\text{Sum of Excess Expenditures}}{\text{Number of Measurement Dates}} = \frac{200,000 + 800,000 + 0 + 0}{4} = \$250,000$$

Calculate average excess expenditures for Unit B:

Unit B	03/31/2015	06/30/3015	09/30/3015	12/31/2015
APEs	\$ 0	\$ 500,000	\$ 1,000,000	\$ 1,600,000
Traced Debt	\$ 0	\$ 0	\$ 0	\$ 0
Excess Exps.	\$ 0	\$ 500,000	\$ 1,000,000	\$ 1,600,000

$$\frac{\text{Sum of Excess Expenditures}}{\text{Number of Measurement Dates}} = \frac{0 + 500,000 + 1,000,000 + 1,600,000}{4} = \$775,000$$

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 6: Apply the Avoided Cost Method (cont'd)

Sub-step C: Compute the excess expenditure amount for each unit of property. (cont'd)

Calculate interest incurred on nontraced debt during the computation period:

Loan #	Principal	Annual Rate	Monthly Interest	# months outstanding	Interest Incurred
1	\$ 1,000,000	9%	\$ 7,500	8	\$ 60,000
2	\$ 2,000,000	11%	\$ 18,333	7	\$ 128,333
				Total	\$ 188,333

Total Amount of Interest Incurred During the Computation Period on All Eligible Debt	=	\$ 188,333
(-)Total Amount of Interest Incurred During the Computation Period on Traced Debt	=	\$ (45,000)
Interest Incurred on Nontraced Debt During the Computation Period		143,000

Calculate average nontraced debt for the computation period:

Debt Type	03/31/2015	06/30/2015	09/30/2015	12/31/2015
Eligible Debt	\$ 1,000,000	\$ 3,000,000	\$ 2,000,000	\$ 2,000,000
Traced Debt	\$ (1,000,000)	\$ (1,000,000)	\$ 0	\$ 0
Nontraced Debt	\$ 0	\$ 2,000,000	\$ 2,000,000	\$ 2,000,000

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 6: Apply the Avoided Cost Method (cont'd)

Sub-step C: Compute the excess expenditure amount for each unit of property (cont'd)

Calculate the weighted average interest rate:

$$\frac{\text{Interest Incurred on Nontraced Debt During the Computation Period}}{\text{Average Nontraced Debt for the Computation Period}} = \frac{143,000}{1,500,000} = 9.56\%$$

Calculate the excess expenditure amount for each unit of property:

Unit A	\$ 250,000	x	9.56%	=	\$ 23,900
Unit B	\$ 775,000	x	9.56%	=	\$ 74,090

Sub-step D: Compute the total interest available to be capitalized:

Interest incurred on nontraced debt during the computation period	=	\$ 143,333
Interest incurred on borrowings described in Treas. Reg. 1.263A-9(a)(4)(iii)	=	0
(Partnerships) Guaranteed payments for the use of capital	=	0
Total interest available to be capitalized	=	\$ 143,333

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 6: Apply the Avoided Cost Method (cont'd)

Sub-step E: Compare sum of excess expenditure amounts for all units of property to total interest available to be capitalized:

Sum of Excess Expenditure Amounts		Total Interest Available to Be Capitalized	
Unit A	=	\$ 23,900	
Unit B	=	<u>\$ 74,090</u>	
Total	=	\$ 97,090	< \$ 143,333

Corporation X has enough interest to capitalize the excess expenditure amounts for all units of property.

Conclusion: Total amount of interest capitalized to each unit of property for the computation period

<u>Traced Debt Amount</u>			<u>Excess Expenditure Amount</u>		=	<u>Total</u>
Unit A	45,000	+		23,900	=	\$ 68,900
Unit B	0	+		74,090	=	\$ 74,090

Examples of the Process (cont'd)

Interest Capitalization for Self-Constructed Assets

Description

Step 7: Impose a Change of Accounting Method

If the taxpayer's current method of accounting for interest does not comply with IRC 263A(f) either by failing to capitalize any interest for Unit A and Unit B or by under capitalizing the interest amount, the taxpayer is using an impermissible method of accounting. Therefore, impose an accounting method change as described in Step 7 of this practice unit.

Other Considerations / Impact to Audit

Interest Capitalization for Self-Constructed Assets	
Considerations	Resources
<ul style="list-style-type: none"> Consider the proper capitalization of other IRC 263A costs to the property; e.g., direct production costs of the asset, indirect costs (such as employee benefits), engineering and design costs, officer compensation, other mixed and administrative costs. 	<ul style="list-style-type: none"> Issue Snapshot - <i>Identifying and Allocating the Costs of Self-Constructed Assets under IRC 263A</i> Issue Snapshot - <i>263A Costs and Allocation Methods</i>
<ul style="list-style-type: none"> Custom homebuilder costs require capitalization, e.g., indirect costs such as officer compensation, insurance or employee benefits. 	<ul style="list-style-type: none"> Issue Snapshot - <i>263A Custom Homebuilders</i>
<ul style="list-style-type: none"> Once interest capitalization applies, depreciation should be updated due to the change in the basis of the asset. 	

Index of Referenced Resources

Interest Capitalization for Self-Constructed Assets
IRC 263A
IRC 446
IRC 453A
IRC 460
IRC 481(a)
IRC 707(c)
IRC 1274(d)
Treas. Reg. 1.163A-8T
Treas. Reg. 1.263A-2(a)(1)(i)
Treas. Reg. 1.263A-8
Treas. Reg. 1.263A-9
Treas. Reg. 1.263A-10
Treas. Reg. 1.263A-11
Treas. Reg. 1.263A-12
Treas. Reg. 1.446-1
Treas. Reg. 5c.168

Index of Referenced Resources (cont'd)

Interest Capitalization for Self-Constructed Assets
Rev. Proc. 2002-18
Rev. Proc. 2015-13
Notice 88-99
<i>Further Consolidated Appropriations Act, 2020</i>
<i>Tax Cuts and Jobs Act</i>
Issue Snapshot - <i>Basic Method of Accounting Concepts</i>
Issue Snapshot - <i>Involuntary (Service-Initiated) Method Change</i>
Issue Snapshot - <i>IRC 481(a)</i>
Issue Snapshot - <i>IRC 481(b) Tax Limitation</i>
Issue Snapshot - <i>263A Costs and Allocation Methods</i>
Issue Snapshot - <i>263A Custom Homebuilders</i>
Pro Forma - Unauthorized Method Change Issue Notice of Proposed Adjustment
Pro Forma - Service-Imposed Method Change Notice of Proposed Adjustment

Training and Additional Resources

Interest Capitalization for Self-Constructed Assets	
Type of Resource	Description(s)
Saba Meeting Sessions	▪ Basic Concepts of UNICAP and Self-Constructed Assets PPT - 2015-07
Issue Toolkits	▪ Issue Snapshot - <i>Capitalizable Interest</i> ▪ Issue Snapshot - <i>Partnership Interest Capitalization</i>
Other Training Materials	▪ Job Aid - <i>IRC 263A Uniform Capitalization Reference Guide</i>

Glossary of Terms and Acronyms

Term/Acronym	Definition
AFR	Applicable Federal Rate
APEs	Accumulated Production Expenditures
CAM	Change in Accounting Method
Excess Exps	Excess Expenditures
IRC	Internal Revenue Code
Rev. Proc.	Revenue Procedure
Treas. Reg.	Treasury Regulation
UNICAP	Uniform Capitalization

Index of Related Practice Units

Associated UIL(s)	Related Practice Unit	DCN
	None at this time.	