



OFFICE OF  
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DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

March 3, 2009

Number: **INFO 2009-0130**

Release Date: 9/25/2009

CC:PSI:5:  
CONEX-104482-09  
U.I.L.: 174.05-00

Dear \_\_\_\_\_ :

This is in response to your letter, dated December 22, 2008, on behalf of \_\_\_\_\_ (Taxpayer), in which you seek to adopt the method described in section 174(a) of the Internal Revenue Code to treat research and experimental expenditures (R&E expenditures) relating to Taxpayer's development of \_\_\_\_\_ as deductible expenses and not chargeable to capital account. The following information is provided to you pursuant to section 2.04 of Revenue Procedure 2009-1, 2009-1 I.R.B. 1 (January 5, 2009). This information letter is advisory only and has no binding effect on the Internal Revenue Service (IRS).

Section 174(a) provides that a taxpayer may elect to treat R&E expenditures as expenses not chargeable to capital account. Expenditures to which the election applies are allowed as a deduction. A taxpayer may elect this method without the consent of the Secretary of the Treasury for the taxpayer's first taxable year in which R&E expenditures are paid or incurred. If the taxpayer elects this method, the method will apply to all R&E expenditures paid or incurred by the taxpayer for the tax year and must be adhered to for all subsequent years unless, with permission of the Secretary, a change is authorized for all or part of such R&E expenditures. The statute also provides that a taxpayer may adopt this method at any time with the consent of the Secretary.

Section 174(b) provides that a taxpayer may elect, under regulations, to amortize (treat as deferred expenses) R&E expenditures over a period of not less than 60 months. The taxpayer may elect this method without the consent of the Secretary for the taxpayer's first taxable year in which R&E expenditures are paid or incurred. If the taxpayer elects this method, the method and the period selected must be adhered

to for the tax year of the election and all subsequent years unless, with the approval of the Secretary, a change is authorized with respect to part or all of such R&E expenditures. The election under section 174(b) will not apply to any expenditure paid or incurred in a tax year before the year for which the election is made.

Section 1.174-1 of the Income Tax Regulations provides that, if the taxpayer does not elect to expense under section 174(a) or defer and amortize expenses under § 174(b) for the first taxable year in which R&E expenditures are paid or incurred, R&E expenditures must be charged to capital account. Section 1.174-1 also clarifies that R&E expenditures to which § 174 applies may relate to a general research program or to a particular project.

Section 1.174-3 of the Income Tax Regulations provides rules for making the election to expense R&E expenditures under § 174(a) and for requesting permission to change to or from that method. Section 1.174-3(a) provides that if a taxpayer adopts the method provided in § 174(a), the method applies to all R&E expenditures paid or incurred in the taxable year of adoption and all subsequent taxable years unless a different method is authorized by the Commissioner of Internal Revenue under § 174(a)(3) with respect to part or all of the R&E expenditures. Section 1.174-3(b) provides that the consent of the Commissioner is not required if the taxpayer adopts the method for the first taxable year in which he pays or incurs R&E expenditures. However, if the taxpayer fails to adopt the method for the first taxable year in which the taxpayer incurs R&E expenditures, the taxpayer cannot do so in subsequent taxable years without obtaining the consent of the Commissioner. In addition, a taxpayer may not use, in the same tax year, more than one method for any particular project.

In Revenue Procedure 2008-52, I.R.B. 2008-36 (September 8, 2008), the IRS provides procedures under which a taxpayer may obtain the automatic consent of the Commissioner to change certain methods of accounting. Appendix section 7.02 of Revenue Procedure 2008-52 includes procedures for taxpayers to obtain automatic consent to change their treatment of R&E expenditures. The URL for the Revenue Procedure 2008-52 is [http://www.irs.gov/irb/2008\\_36\\_IRB/ar09.html](http://www.irs.gov/irb/2008_36_IRB/ar09.html). Also, Appendix section 7.02(b) provides information regarding a change in the treatment of computer software costs under Revenue Procedure 2000-50, 2000-2 C.B. 601, as modified by Revenue Procedure 2007-16, 2007-4 I.R.B. 358 (but see section 9 of the appendix for making that change).

This letter should not be regarded as a private letter ruling, nor relied upon as such. If you have any questions, you may contact \_\_\_\_\_ at \_\_\_\_\_.

Sincerely,

Paul F. Handleman  
Chief, Branch 5  
Office of Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosure