



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

OFFICE OF THE CHIEF COUNSEL

November 29, 2012

Number: **2012-0070**
Release Date: 12/28/2012

CONEX-146800-12

UIL: 168.35-00

The Honorable Bob Goodlatte
Member, U.S. House of Representatives
117 South Lewis Street, Suite 216
Staunton, VA 24401

Attention:

Dear Congressman Goodlatte:

I am responding to your inquiry dated October 23, 2012, on behalf of your constituent, _____, a small business owner, wrote about the temporary and proposed regulations on the tax treatment of amounts paid to acquire, produce, or improve tangible property under sections 162 and 263(a) of the Internal Revenue Code (the Code) and on the accounting for, and disposition of, property subject to section 168 of the Code (the "temporary regulations").

_____ provided two examples to illustrate her concerns. In the first example, she said that the temporary regulations require a taxpayer to capitalize and depreciate a \$1.99 wastebasket that a taxpayer uses in his or her business because the temporary regulations do not provide a deduction for a de minimis amount of immaterial expenses. Under the temporary regulations in section 1.162-3T, this wastebasket is a material and supply because it has an acquisition cost of \$100 or less. If the taxpayer does not take a physical inventory of wastebaskets at the beginning and end of the taxable year, he or she should deduct the \$1.99 wastebasket as an incidental material and supply in the year in which he or she paid that amount. If the taxpayer does take a physical inventory of wastebaskets, he or she should deduct the \$1.99 wastebasket as a non-incidental material and supply in the year in which he or she begins to use the wastebasket.

In the second example, _____ said that a taxpayer will need to perform a cost

segregation study to allocate a portion of the cost of a building to a HVAC unit that the taxpayer replaced. The temporary regulations allow the taxpayer to deduct any remaining adjusted basis in the old HVAC unit. If the taxpayer includes the cost of the old HVAC unit in a building's overall costs and does not break it out separately, the temporary regulations allow the taxpayer to use any reasonable method to estimate the cost of the old HVAC unit. The temporary regulations do not require that the taxpayer perform a cost segregation study to estimate these costs.

The IRS and the Treasury Department received numerous comments on the temporary regulations, and a number of commentators pointed out the administrative burden that the temporary regulations impose on small businesses. As a result, the IRS and the Treasury Department are considering providing additional relief for small businesses in the final regulations, which we expect to publish in 2013. In addition, the IRS announced on November 20, 2012, in Notice 2012-73, that it would change the effective date of the temporary regulations to taxable years beginning on or after January 1, 2014.

I hope this information is helpful. If you need further assistance, please call me or
at .

Sincerely,

Kathleen Reed

Kathleen Reed
Branch Chief, Branch 7
Office of Associate Chief Counsel
(Income Tax & Accounting)