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From:

Sent: Tuesday, March 15, 2016 10:33:51 AM

To:

Cc: [REDACTED]

Bcc:

Subject: Question Re: Audit Protection For Tangibles Method Changes

Recently, you posed a question regarding audit protection for changes under the final tangible property regulations. Specifically, you asked whether a taxpayer that makes an automatic change in method of accounting to utilize the final tangible regulations pursuant to section 10.11 of Rev. Proc. 2015-14, 2015-5 I.R.B 450, and takes into account the limited § 481(a) adjustment for that change as required by section 10.11(6)(b)(i) of that revenue procedure, should have audit protection for that item in taxable years prior to the year of change, or at least prior to the date that amounts paid or incurred for the item may be included in the § 481(a) adjustment. Your example involved a taxpayer that made an automatic change for its taxable year beginning 1-1-14 under section 10.11(3)(a)(i) to deduct non-incidentals materials and supplies in the taxable year they are used or consumed in accordance with § 1.162-3(a)(1) and (c)(1). Under section 10.11(6)(b)(i) of Rev. Proc. 2015-14, the taxpayer calculated its § 481(a) adjustment taking into account only amounts paid or incurred in taxable years beginning on or after 1-1-14. Your question was: for costs paid or incurred by the taxpayer in taxable years beginning prior to 1-1-14, whether Exam can examine or change the taxpayer's method of accounting for non-incidentals materials and supplies that were deducted when paid or incurred by the taxpayer to the correct method of deducting those items when they were used or consumed in the taxpayer's operations.

Under your example, we believe that the taxpayer has audit protection for the costs of non-incidentals materials and supplies paid or incurred prior to 1-1-14. Section 8.01 of Rev. Proc. 2015-13, 2015-5 I.R.B. 419, provides that, except as otherwise provided in section 8.02 of Rev. Proc. 2015-13 or under any guidance provided in the I.R.B., when a taxpayer timely files a Form 3115, the IRS will not require the taxpayer to change its method of accounting for the same item for a taxable year prior to the requested year of change. Note that section 10.11 of Rev. Proc. 2015-14, addressing automatic method changes under tangible property regulations, does not specifically address audit protection for taxpayers that file method changes under its general provisions or its provisions for automatic changes made with a limited adjustment. Therefore, the general rule under section 8.01 of Rev. Proc. 2015-13 should apply to these changes. If the taxpayer timely filed a Form 3115 for 2014 to change its method of accounting for

non-incidental materials and supplies pursuant to section 10.11(3)(a)(i) of Rev. Proc. 2015-14, and properly included the limited § 481(a) adjustment, then the IRS cannot require the taxpayer to change its method of accounting for its non-incidental materials and supplies costs incurred prior to the year of change.

For the same reasons, if a taxpayer made an automatic change in method of accounting to utilize the final tangible regulations pursuant to section 10.11 of Rev. Proc. 2015-14, 2015-5 I.R.B. 450, and that change was made with the limited § 481(a) adjustment required under section 10.11(6)(b) of that revenue procedure, this taxpayer cannot request a subsequent or additional method change for the same item, but only for costs paid or incurred prior to taxable years beginning prior to 1-1-14. For these purposes, we believe the taxpayer would have already made the appropriate method change for all costs paid or incurred for these items, and the taxpayer would have taken into account the appropriate § 481(a) adjustment for these items, regardless of the taxable year in which such costs were incurred. As with any change in method of accounting under the final tangible property regulations, a taxpayer that desires to change its method of accounting for any item that it previously changed under section 10.11 of Rev. Proc. 2015-14 or for any item that it has not yet changed under section 10.11, must change to a method under the final tangible property regulations using the procedures under Rev. Proc. 2015-13 and Rev. Proc. 2015-14 (but only if the taxpayer meets the eligibility requirements for an automatic change), and the taxpayer must include a § 481(a) adjustment as appropriate under the final tangible property regulations.

I hope that this information was helpful. If you need additional information, please give me a call.