

TAX NEWS BRIEFING

IMPORTANT CHANGES TO THE IRS REPAIR REGULATIONS

February 20, 2015

Background

The tangible property regulations (“Repair Regs”) are a consideration that have not received much attention until the past couple weeks. The regulations help distinguish capital expenditures from supplies, repairs, maintenance, and other deductible expenses. Virtually every business that acquires, produces, or improves tangible property must comply with these new rules for the tax year beginning on or after January 1, 2014.

The new rules are “taxpayer friendly” from the standpoint of providing guidance for accelerating deductions for certain tangible property expenses under new criteria for treating expenses as materials and supplies, repairs and maintenance, or improvements to tangible property.

Although the Regulations impact virtually every business, starting January 1, 2014, we have been provided very little practical guidance and have not had access to in-depth training.

In October 2014 Members of Congress Rice and Murphy sent a letter to the IRS Commissioner requesting relief for small business. [Repair Regulations Letter to IRS from Rice and Murphy](#).

Early in 2015 the IRS issued [Rev. Proc. 2015-14](#), a 393 page document that modified previous implementation procedures. 2015-14 requires most businesses receive consent with the IRS to change their accounting methods and to retroactively apply the Repair Regs to years prior to January 1, 2014. Additionally, the procedures require most businesses to compute a catch-up adjustment, then complete and file Form 3115 to report the adjustment and compliance with the new regulations.

After digesting [Rev. Proc. 2015-14](#), the business community and tax professionals were very concerned about complying with the procedures for several reasons:

1. The IRS is requiring taxpayers to ask for permission to change their accounting methods to conform to the new Repair Regs the IRS themselves made mandatory,
2. Taxpayers (including RHCPAS clients) previously followed procedures acceptable by the IRS when determining what to expense and what to capitalize. The Repair Regs re-wrote the rules, so why would businesses have to go back and change something they were doing correctly?
3. Although the final tangible property regulations are favorable to most businesses, retroactive compliance is a huge burden. The procedures require businesses to:

- a. Review asset repair records and determine if any previously expensed repairs would require capitalization under the tangible property regulations, and
- b. Review repairs that were previously capitalized and determine if they should be expensed under the new regulations.
- c. Change the method of accounting for the identified items, calculate the adjustment and account for it on Form 3115. Note the adjustment could either create taxes or tax savings.

In the case of a building, this could require a business to go back as far as 38 years!

4. Compliance with the Repair Regulations is already going to increase the cost of tax preparation. Retroactive application will come with a very large price tag and in most cases will have no value to the business.

The procedures created uproar among tax professionals. The American Institute of Accountants, many State CPA Organizations and other associations representing Tax Professionals started writing and calling the IRS to express concern about the hardship this would cause. The procedures began to get national media attention in February:

On February 2, 2015 Forbes contributor Peter J Reilly highlighted the fact that the IRS estimates compliance will require “38 hours 29 minutes of record keeping, 19 hours and 54 minutes to learn about the law and 23 hours and 48 minutes to prepare and send the form to the IRS. ([Repair Regs and Tax Pros Are Like Headlights and Deer](#)).

On February 10, 2015 Peter J Reilly wrote in another article ([Repair Regs – A hellish Tax Season and Refunds of Biblical Magnitude](#)): “Have you ever [heard of Form 3115](#)? Go ahead and take a look at the eight page form, that’s why I gave you a link. Now take a look at the [twenty pages of instructions](#). Scroll to the very end where there is an estimate of the burden that the form puts on the taxpayers as required by the Paperwork Reduction Act.”

In the Preamble to the final tangible property regulations the IRS estimated total **annual** reporting burden will be approximately 1,100,000 hours.

RHCPAS perspective: The Repair Regs require a significant investment in time and talent to assure compliance. We believe learning *how to* comply will require approximately 40 hours per professional. The time needed to actually comply will vary based on facts and circumstances.

Relief came for small businesses on February 13th

The IRS released [Rev. Proc. 2015-20](#), which is immediately effective. The procedure permits small businesses to:

- Change their methods of accounting under the final tangible property regulation on a prospective basis, i.e. beginning on January 1, 2014,
- Avoid completing and filing Form 3115.

The procedure is available to businesses with assets totaling less than \$10 million or gross receipts averaging \$10 million or less in the past three years.

We believe these procedures will reduce the administrative compliance and cost for many of our small business clients.

Considerations and next steps

Developments relating to these regulations are changing in real time. Please be patient, what we discuss today could change tomorrow. As an example:

The IRS allows a De Minimis expensing election whereas taxpayers that have their financial statements audited can deduct amounts paid to acquire or produce property if those amounts are less than \$5,000. Taxpayers with unaudited financial statements have a lesser safe harbor of \$500. In [Rev. Proc. 2015-20](#) the IRS has asked for public comment on the appropriateness of these amounts. After analysis the IRS may increase the safe harbor amounts later this year.

We believe these mandatory Repair Regs and IRS procedures apply to all businesses. Our team is dedicated and trained to help you implement these rules in order to provide the best benefit. We will be contacting you to discuss the impact on your business and develop an implementation plan specific to your facts and circumstances. We believe all businesses will follow one of these implementation paths:

1. **Your business qualifies for the small business exemption and retroactive application will have no value:** In these cases, we will work with you to ensure expenditures after January 1, 2014 comply with the regulations and file your return with the new required disclosures and elections as soon as possible.
2. **Your business qualifies for the small business exemption and retroactive application may create value:** In these cases, we are recommending extension of the returns to await additional relief, guidance and training.
3. **Your business does not qualify for the small business exemption:** In these cases, we are recommending extensions of the return to await additional relief, guidance and training.

As the IRS and our profession issue additional guidance we will share that with you.

Please ask questions -

Contact information

Chad Harty
Tax Manager
charty@rhcpas.com
(248) 598-5030

Brian Hare
Director
Brian@rhcpas.com
(248) 598-5030

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