# Updated Procedures Related To Deducting And Capitalizing Business Expenses

By Jim Griffing, A Silver Fox Advisor

We want to update you on a recently released IRS procedure (Rev. Proc. 2015-20) which modifies the final regs we emailed you about last week. The service eased the requirements for certain small taxpayers by giving them the option of not filing the Application for Change in Accounting Method, Form 3115. A small taxpayer is defined as a business with less than $10 million in total assets or average annual gross receipts of $10 million or less for the prior three taxable years. All businesses (including sole proprietorships and rental real estate owners) will still be required to follow the new accounting requirements relating to the way a taxpayer must evaluate certain expenditures in order to determine whether the costs represent immediately deductible repair expenses or capital improvements that must be depreciated over time. In addition, the IRS regulations provide new guidelines on when a taxpayer may deduct costs incurred to acquire "material and supplies"; however, the small taxpayer will have the option to file Form 3115 or not.

Part of the preparation of Form 3115 involves calculating changes to prior years based on if these new rules had been in place previously. For some businesses, this will provide a chance to expense on their 2014 tax return some prior year assets which are currently being depreciated. Others would see no such savings and therefore choose to forego the expense of preparing the form. If requested, we will evaluate each small taxpayer return we prepare and suggest including Form 3115 if we find that it will provide that client with a lower current year taxable income.

RECAP: Rev. Proc. 2015-20 provides relief to a small taxpayer by not requiring them to file a Form 3115 and by not requiring them to go back and review prior years based on the new rules. Instead, the taxpayer can choose to apply the regulations for only those expenses incurred after January 1, 2014. If your business could stand to benefit from even one immediate write-off of a prior asset, all prior years must be evaluated as well or else risk losing expenses under the "use it or lose it rule".

All of our tax clients need a written policy which they should have adopted so that their accounting will be in compliance with IRS requirements. We can send samples of policies, if requested.

**New Regs Required Evaluation of Materials and Supplies**: There are three types of materials and supplies, and it is the nature of the item that drives when it may be deducted under the final regulations. Under the final regulations, every repair cost must be evaluated through a series of steps that will yield the proper treatment of the cost: capitalize or deduct. First, there are the three safe-harbors annual elections that you can avail yourself of in the final regulations: the $5,000/$500 De Minimis safe harbor, the small building safe harbor, or the routine maintenance safe harbor. If you can't use the safe harbors, then you have to run your repair costs through a multi-step test. Part of this test will determine whether the cost represents a Betterment, Restoration, or Adaptation for a New or Different Use. If it does, the cost must be capitalized; if it does not, you can expense the cost.

Please contact us for additional information, an evaluation or samples of written policies. ♦

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