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Implementing the Final Repair Regulations

Late in 2013, the IRS released final regulations regarding expenditures to acquire, produce or improve tangible property. These regulations are commonly referred to as the "repair regs" and were effective January 1, 2014. Below is a summary of steps to take to comply with these new regulations.

1 - Have a capitalization policy in place.

Taxpayers with an applicable financial statement have a special de minimis expensing rule. These taxpayers can follow their book treatment if written accounting procedures are in place for expensing amounts paid under a certain dollar amount. The amount paid may not exceed $5,000 per invoice or per item as detailed on the invoice. For small taxpayers without any type of audited financial statement, any expenditure over $500 per invoice or item must be capitalized.

In order to utilize this safe harbor, a written capitalization must be in place as of the beginning of the year. The safe harbor is elected annually by including a statement with the taxpayer's timely filed return.

If a taxpayer does not have a written capitalization policy in place, any expenditure over $200 must be capitalized.

2 - Review all expenditures above your capitalization policy.

Make sure you have an understanding of the new regulations and what is considered a unit of property and requires capitalization. If the expenditure is a betterment or restoration, this may qualify for expensing rather than capitalization.

Please refer to our summarization of the final regulations to help guide you on this decision or consult with us for further guidance.

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3 - Review current year dispositions.

Taxpayers may forgo a loss upon the disposition of a structural component and expense the related repairs in certain instances. If the taxpayer desires instead to take a loss on a disposed component, then a partial disposition election must be made. This election is made on a taxpayer's timely filed return.

4 - Review depreciation schedules for prior year retirements.

Identify all prior year retirements that are still capitalized. This generally occurs anytime an existing building or machine is improved or renovated as older components are demolished or removed to accommodate new ones. In addition to claiming immediate retirement deductions, this process will also eliminate paying recapture tax on §1245 and §1250 building components that no longer exist.

5 - Make timely elections on 2014 returns.

- Capitalization safe harbor election (see previous discussion).
- Partial disposition election (see previous discussion)
- Safe harbor election for small taxpayers. Please see our summarization of the final regulations for a complete discussion on qualifying as a small taxpayer.

6 - Revoke prior General Asset Account Election.

If a general asset account ("GAA") election was made under the temporary regulations, it may be beneficial to file Form 3115 to revoke this election under the final regulations.

7 - File Form 3115 on a timely basis.

Many taxpayers will need to file Form 3115 to comply with the new regulations. In many cases, the 481(a) adjustment will be zero as the regulations are mandatory as of January 1, 2014. The form is due by the due date for timely filing your return.

Taxpayers can make the automatic method changes on one Form 3115 as long as specific information for each change is disclosed. Larger taxpayers may need to complete Form 3115 in greater detail. Please contact us if you need assistance in completing this form.