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## **Changes to repairs require changes in methods**

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A year has gone by and CPAs and other professionals have been able to digest the new regulations as to if repairs should be capitalized or deducted. In late 2013, the IRS released final repair versus capitalization regulations. These new regulations gave taxpayers something more concrete in determining if repairs should be capitalized or deducted. These regulations are far reaching and will affect every taxpayer that holds tangible property. Finally in August of 2014, the IRS issued Finalized regulations on the disposition of retired assets.

Taxpayers and CPAs were warned that the rules were applicable for tax years beginning on or after January 1, 2014, but many of the transition rules were not released until January of 2014 with additional guidance in September of 2014. While the new regulations will affect virtually every taxpayer holding tangible property, the transition rules will require all those taxpayers affected to file for automatic changes in accounting methods. This will cause increased reporting and compliance with the laws.

While there may be an increase in time and cost to prepare taxpayers' 2014 tax returns, there are a number of benefits to these new rules. These rules should reduce controversy over what was deductible as a repair and what had to be capitalized. In many instances they give us support for deducting some of things that were standard practice in the past from liberal IRS regulations and court cases.

Some of the major highlights of the final regulations include new safe harbors to deduct routine maintenance items on buildings, an election to capitalize repairs and maintenance items in accordance with financial statements, a de minimis safe harbor to deduct items under \$5,000/\$500 and a small taxpayer safe harbor.

Under the disposition regulations, taxpayers can now take a loss on disposed of building components. For example, if a taxpayer replaces their HVAC system, they may take a loss on the remaining basis of the old HVAC system. This is even the case for past years. If the taxpayer replaced the HVAC system in 2010, but is still depreciating two HVAC systems, the new rules allow you to go back and write off the old HVAC system. There are some tricky rules in calculating and allowing these write offs, especially from prior years. Prior year disposals may only be taken in tax year 2014. The IRS is allowing taxpayers one chance to deduct these prior dispositions. Going forward, taxpayers will only be able to write off dispositions in the year the asset is actually disposed.

Applying all of these new rules will require changes in accounting methods. However, most taxpayers will not have a choice. The IRS is requiring us to comply with these rules, while at the same time they are telling us we need to change our accounting methods in order to comply. Most, if not every, taxpayer that owns tangible property will be required to file at least one Form 3115 (Application for Change in Accounting Method). The IRS is telling us that they will be looking at

taxpayers with tangible property that have not complied with these new rules by filing method changes. Many of these filing will require discussions between the CPA and the taxpayers to accurately report the information.

The implementation of these final regulations was required for tax years beginning on or after January 1, 2014. With the 2015 filing season coming in January, taxpayers and their CPAs should be having conversations as to how these will alter their 2014 tax returns and at what additional cost. Due to this quick timing, taxpayers should be consulting with their tax advisors now to ensure there are no missed requirements or opportunities.

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