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▶SUBJECT
TEMPORARY REGULATIONS REGARDING DEDUCTION AND CAPITALIZATION OF EXPENDITURES RELATED TO TANGIBLE PROPERTY

▶SUMMARY
The temporary regulations provide guidance to taxpayers on costs paid to acquire, produce, or improve tangible property. Taxpayers often capitalize such costs, even though those costs are otherwise deductible as repair or maintenance costs.

▶DETAILS
On December 23, 2011, the Internal Revenue Service released temporary regulations on the treatment of certain costs incurred in connection with tangible property. Because the regulations provide authority for the deduction of certain of these costs as repairs, the regulations have been informally referred to as the "repair" regulations. The regulations were issued in temporary and proposed form, and are expected to be issued in final form after the expiration of a comment period and after a hearing (if requested) has been held. These regulations provide guidance on many of the provisions of the 2008 proposed regulations, adopting guidance on the general rules for capital expenditures, acquisition or production of property, and improvement of tangible property.

The temporary regulations also refined guidance for materials and supplies, the de minimis rule, and the safe harbor for routine maintenance. Further, the temporary regulations modified some of the rules set out in the 2008 proposed regulations. The modified rules discuss, among other areas, 1) the definition of a unit of property, 2) whether there has been an improvement to a unit of property,

▶Read more

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3) whether an amount paid is for an improvement to a building, 4) replacement of a major component or substantial structural part of a unit of property, and 5) disposition of property. The temporary regulations also included revisions to loss recognition rules, which now permit taxpayers to claim losses on the disposition of a structural component of real property.

These regulations are generally effective for taxable years beginning on or after January 1, 2012.

OPPORTUNITIES FOR TAXPAYERS

Where a taxpayer originally capitalized costs otherwise deductible under these regulations, an opportunity may exist to deduct such costs. Two revenue procedures are expected to be issued by the Service, providing additional guidance on the implementation of these temporary regulations. To implement a change to comply with these regulations, Form 3115, Application for Change in Accounting Method, must be filed. This is an automatic change that does not require advance consent of the Service. A section 481(a) "catch-up" deduction will capture the missed deductions in the year of the method change.

Additional guidance on these new regulations will be provided in a subsequent, more detailed release and webcast.

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