

Dear Clients and Friends of the Firm:

IRS REPAIR/CAPITALIZATION REGULATIONS FINALIZED

Effective January 1, 2014, the IRS has released the much-anticipated final “repair” regulations governing when taxpayers must capitalize and when they can deduct their expenses for acquiring, maintaining, repairing and replacing tangible property. Compliance with these regulations will impact virtually every business with tangible property. Among the material changes contained within the regulations are:

- Revised and simplified safe harbor election for deducting materials and supplies that have a useful life over one year, but cost under \$5,000 for taxpayers with audited financial statements and under \$500 for all other taxpayers.
- Safe harbor provision for routine maintenance on buildings, allowing a deduction for maintenance that is expected to be performed more than once over a ten year period.
- Annual election for small taxpayers with buildings to immediately deduct repairs, maintenance and improvement items up to \$10,000 or 2% of unadjusted basis per year.
- Refined criteria for defining betterments and restorations to fixed assets in order to determine whether these expenditures can be immediately expensed vs. capitalized.
- Partial disposition election allowing taxpayers to immediately deduct a loss on the retirement of structural components when a replacement cost for that component has been capitalized.

In order to comply with these regulations, all taxpayers who own tangible property such as a building or equipment will be required to file Form 3115, “Application for Change in Accounting Method” with its 2014 income tax return. This applies to all taxpayers regardless of entity structure including individuals, businesses and trusts.

Form 3115 is complex and the amount of time required to complete this form will vary among taxpayers but will increase the cost of tax return compliance for 2014. Whether the adoption of these regulations produces a favorable or unfavorable tax impact will also vary among taxpayers depending on the facts.

Recently, the American Society of CPAs (AICPA) along with several different State Board of Accountancy organizations requested that the IRS consider granting some taxpayer relief from the administrative burden and added cost of compliance with these new regulations. If any positive developments emerge from these efforts, we will let you know immediately.

Should you have any questions regarding the application of these new regulations, please contact us at (951) 445-4700. We will be happy to discuss them in more detail.

Sincerely,

Swenson Advisors, LLP