

Chapter 3:

Tax Accounting Issues

Capitalization Issues

3-1

***Gibson & Assocs.
v.
Comm'r.***

Infrastructure Repairs
are
Capital Expenditures

3-1

Repairs

vs.

Capital Expenditures

3-2

Bridge Components:

- **joints**
- **bearings**
- **stiffeners**

“renovations of major components often extended the useful life of the structures as a whole . . .”

3-2

Rev. Proc. 2011-27
Rev. Proc. 2011-28

3-3

Safe Harbors for
Capitalizing
Telecom Assets

Safe Harbors:

3-3

“Unit of Property”

**“Network Asset
Maintenance
Allowance”**

3-4

Rev. Proc. 2011-29

Safe Harbors for
Capitalizing
Success-Based Fees
in
Business Acquisitions

3-4

*Fees
contingent on
the
successful closing
of a
business acquisition*

Issue:

3-4

**How much
of the fee
is allocable to activities
that do not
“facilitate”
the transaction?**

Safe Harbor:

3-4

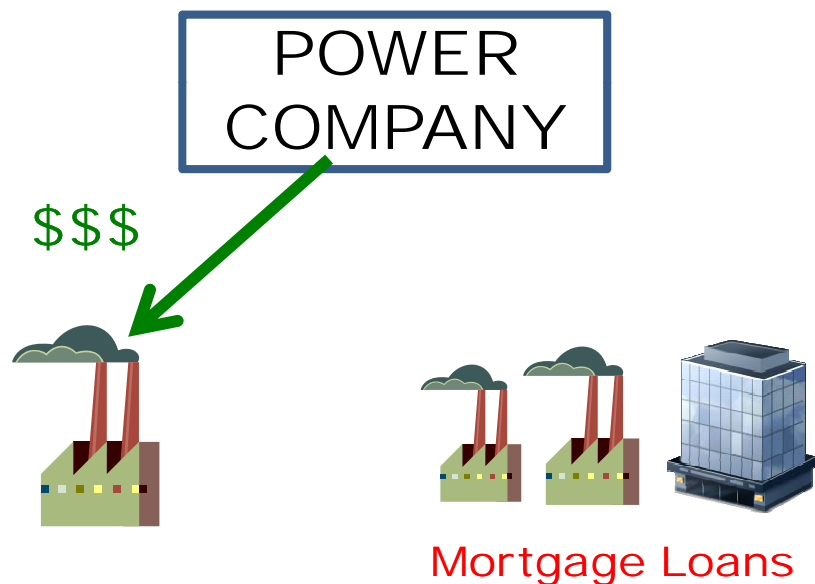
**Deduct 70%
Capitalize 30%**

Dominion Resources v. U.S.

Capitalization of
Interest Expense
for
"Associated Withdrawn
Property"

Sec. 263A(f) "Avoided Cost" Method for Interest Capitalization

Sec. 263A(f) "Accumulated Production Expenditures"



3-5

**Accumulated
Production Expenditures:**

**Includes
Cost of Property
Temporarily
Withdrawn from Service
to
Complete the Construction**

3-6

De Minimis Rule:

**Accumulated
Production Expenditures
Will Not Exceed
5% of
Associated Property Costs**

3-6

CCA 201136022

Loan Commitment Fee
is
Part of
Accumulated Production
Expenditures

Loan Commitment Fee:

**Paid Until
the Loan is
Actually
Drawn Upon**

Loan Commitment Fee:

**Amortized
Over the Term
of the
Loan**

Rev. Rul. 81-160

3-7

Capitalization:

- **Amortization deduction during construction period is capitalized, and**
- **Full amount of commitment fee is included in APE for calculating interest capitalization**

3-7

***Recovery Group Inc.
v.
Comm'r***

Covenant
Not to Compete
is

Sec. 197 Intangible

3-7

**Corporation
Redeems
23% Shareholder
and
Has Him Sign a
Covenant not to Compete**

3-7

3-7

“... entered into in connection with an acquisition of an interest in a trade or business **or substantial portion thereof.”**

“... **or substantial portion ...”**

Applies only to the acquisition of **business assets**, as opposed to an interest in the business

3-9

***Final Regs
on
Start-Up
and
Organization Costs***

3-10

Deemed Election:

Taxpayer is deemed to have elected to deduct/amortize start-up/org costs

*i.e. election **out** is required*

3-10

**Calculation Error
for
2 or More Years
is an
Erroneous
Accounting Method**

3-10

**Calculation Error
for
2 or More Years:**

- **omitted costs**
- **wrong start date**

**Form 3115
is required to correct.**

3-11

**Start-Up & Organization
Costs:**

**When does
business begin?**

Depreciation

3-12

Broz v. Comm'r

MACRS Life
Determination
under
Rev. Proc. 87-56

3-13

PLR 201131010

Underground Pipeline
gets
7-Year
MACRS
Life

3-14

CCA 201123001

Truck Stop
Building
gets
15-Year
MACRS Life

3-15

PLR 201103006

Mixed-Use
Condo
gets
27.5-Year
MACRS Life

Web

CCA 2011147025

Continuing Care
Retirement Community
Buildings
get
27.5-Year
MACRS Life

Web

Types of Units:

- **Independent Living**
- **Assisted Living**
- **Alzheimer's Support Care**
- **Skilled Nursing Care**

Web

**Residents pay
a **Monthly Fee**
for the Units
and
a Variety of
Lifecare Services**

3-15

Broz v. Comm'r

Sec. 197
Amortization
Begins Upon
Start of
Trade or Business

3-16

Douglas v. Comm'r

Airplane
Not
Placed in Service
Without
Pilot to Fly It

3-17

PLR 201105023

Taxpayer
Allowed to
Revoke
Election Out
of
Bonus Depreciation

Accounting
Methods

3-17

Rev. Proc. 2011-14

Updated
Guidelines
for
Automatic Accounting
Method
Changes

New Automatic Change:

Deduction of 3-17
Cal Franchise Tax
by
Accrual Method
Corporations

Rev. Proc. 2011-18

Deferral 3-18
of
Income Recognition
from
Sales of
Gift Cards

Rev. Proc. 2011-17

Accounting 3-18
for
Gift Cards
Issued in Exchange
for
Returned Goods

Rev. Proc. 2011-46

New Safe Harbor 3-18
for
Taxpayers
using the
Nonaccrual-Experience
Method of Accounting

- **Professional services**
- **Other service businesses with average annual gross receipts under \$5 million**

3-18

Exclude A/R that will not be collected, based upon past experience

New Safe Harbor:

3-19

“Book Safe Harbor” Method

**95% of Bad Debt Reserve
on
Applicable Financial Statements**

Applicable Financial Statements

- **Audited Financial Statements**
- **F/S Submitted to SEC**
- **F/S Submitted to Other Government Agencies**

3-19

Bosamia v. Comm’r

IRS Disallowance
of
Related Party
Deductions
is
Change of Accounting
Method

Disallowance of Related Party Accrued Expenses

3-19

Sec. 481(a) Adjustment
Allows IRS to Disallow
Full Amount
of
Accrued Fees
for All Prior Years

3-19

CCA 201121001

Timing
of
Deduction
for
Credit Facility Fees

Accrued “Credit Facility Fee” for Guaranteeing Bond

3-20

Payment Liability under
Economic Performance Rules,
because not specifically
covered elsewhere in regs

Other Issues

3-20

TAM 20111004

Involuntary Conversion
of
Inventory
in
Presidentially-Declared
Disaster

3-21

**Inventory
will be treated as
“property held for productive
use in a trade or business”
under
sec. 1033(h)(2)**

3-21

Rev. Rul. 2011-24

IRS Determines
Portion of
**Telecom Company
Gross Receipts**
Eligible for
Sec. 199 Deduction

3-22

Cal. TAM 2011-01

Construction-in-Progress
Not
Included
in
Cal Property Factor