

REPAIRS & MAINTENANCE AND FIXED ASSET CAPITALIZATION REGULATIONS - NEW RULES FOR 2014

The IRS has revised a number of its regulations regarding fixed assets. These rules were issued in 2014 and are over 400 pages long. They affect the following areas: **Materials and Supplies, Repair vs. Capitalization for Equipment, Routine Maintenance for Equipment, Work performed on facilities taxpayers own or rent.**

What all businesses need to do now

- Complete or update your company's written capitalization policy
- Review the new rules by discussing with your CPA firm
- Review 2014 repairs and maintenance expenditures and capitalized fixed assets for items to expense vs. capitalize

Written safe harbor de minimus capitalization policy

- Each taxpayer must have a written policy in place by January 1, 2014
- States the amount of repairs, maintenance, or fixed asset purchases that will be expensed vs. capitalized
- If the taxpayer gets a CPA prepared audited financial statement this De Minimus exception can be up to \$5,000 per item
- All other taxpayers get up to \$500 per item, or, if justified, more
- Written capitalization policy should be reviewed and updated each year
- This policy must be the same for financial (book) purposes and tax
- An election is included on the taxpayer's 2014 income tax return

Sample

Effective January 1, 2014, the ABC Company is instituting a capitalization policy for financial statement and tax purposes that all units of property whose economic useful life is shorter than 12 months OR costs less than \$500 will be treated as a current expense. This is a per item test.

Routine maintenance safe harbor

- Recurring repairs to equipment and facilities.
- Does the Company repair or replace significant items (units) of property more than once during:
 - The piece of equipment's life – for example replace brakes and tires for a truck more than once in 6 years?
 - For a building – painting the exterior of a building more than once in 39 years?
- If your Company has these types of expenditures your Company will need to File Form 3115 "Change in Accounting Method" with your 2014 tax return.

Unit of property

- New rules define "Unit of Property"
- Example – for a building the HVAC system is a unit of property. When deciding whether to expense vs. capitalize an expenditure you look at the HVAC system as the unit. You then determine if you have done the following.
 - Betterment – the unit of property
 - Restoration – the unit of property
 - Adapted – the unit of property

Betterment

- Materially increases the quality, productivity, efficiency or strength of the unit of property
- Examples:
 - 50% increase in the efficiency of a machines output is material
 - 50% decrease in energy costs of a HVAC system is material
 - 10% increase in load capacity is not material

Restoration

- Replacement of a major component or substantial structure of a unit of property
- Examples:
 - Replace 100% of HVAC units – capitalize
 - Replace 20% of HVAC units – expense
 - Replace 50% of the engine components in a truck – capitalize
 - Replace 20% of the engine components in a truck – expense

What to do now

- Complete or update 2014 and 2015 written capitalization policy.
- Discuss with Shannon & Associates – all businesses are unique and have different facts and circumstances.