

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

**ORAL STATEMENT
PRESENTED TO
Internal Revenue Service**

**PUBLIC HEARING:
Proposed and Temporary Regulations (REG-168745-03 and TD 9564), Regarding
Deduction and Capitalization of Expenditures Related to Tangible Property**

May 9, 2012

Good morning. My name is Carol Conjura, and I am a partner with KPMG LLP's Washington National Tax Office, and a Certified Public Accountant. In that role, I provide federal income tax planning and consulting services to taxpayers with respect to tax accounting method and related matters.

My testimony today is on behalf of the American Institute of Certified Public Accountants, and I currently serve as the chair of the organization's Tax Methods and Periods Technical Resource Panel.

The AICPA is the world's largest association representing the accounting profession, with nearly 377,000 members across the country and around the world. The organization has a 125-year history of serving the public interest and its members represent many areas of practice, including business and industry, public practice, government, education and consulting.

The [AICPA submitted written comments](#) on the temporary regulations to the government on April 17th and my comments today will focus on the most important of those.

Administrative Burden and Complexity

The AICPA acknowledges how challenging it is for the government to provide detailed regulations that are both clear and comprehensive in this historically uncertain area of tangible property capitalization and we appreciate the significant effort the government has already

expended. Although the regulations in their current form would help taxpayers apply the capitalization rules to tangible property to a degree, the AICPA remains concerned that the overall approach in them is too complex and administratively burdensome. In our view, this is because the regulations rely heavily on the same “facts and circumstances” based approach that has led to long-standing controversy and uncertainty. More specifically, the regulations fail to provide sufficiently objective principles, they do not provide as many bright line tests as are needed, and they also introduce entirely new sources of complexity, such as with respect to component dispositions. Taxpayers and their advisers will have to devote significant resources to understanding these complex rules and then applying them to common or routine transactions every year, such as the purchase of materials and supplies, and recurring property maintenance activities.

Without the benefit of bright line tests, taxpayers and advisers will be forced to develop their own subjective guidelines to determine whether expenditures result in a betterment or restoration, and it won't be known whether and to what extent the taxpayer's self-developed guidelines coincide with those of the IRS until there is an IRS audit of the tax return. As a result, the regulations in their current form, will likely fall short of achieving the government's main goal as stated in the preamble of providing more certainty and less controversy. Instead, the regulations will place demands on many taxpayers that exceed their limited compliance resources. The need for simplification is particularly pressing for small businesses, which make up the majority of business taxpayers. In this regard, the Joint Committee on Taxation recently

issued statistical information showing that 96% of all business tax returns have \$1 million or less of gross receipts and 99% have \$10 million or less.¹

For these reasons, the AICPA recommends that the government take on the challenge of developing and including in the next set of regulations significantly more bright line tests, objective standards, and safe harbors. While the task is undoubtedly challenging, it is both realistic and feasible, and at a minimum, will achieve long-term results that far outweigh the effort required in the short term.

Amounts Paid to Acquire or Produce Tangible Property – De Minimis Rule – Temp. Treas. Reg. § 1.263(a)-2T(g)

Next, I would like to explain the AICPA’s concerns regarding the de minimis rule of Temp. Treas. Reg. § 1.263(a)-2T(g).

First, the requirement that a taxpayer have an Applicable Financial Statement to be entitled to use the de minimis rule unfairly discriminates against smaller taxpayers and, therefore, the AICPA recommends an alternative test that would allow these taxpayers to use the de minimis rule.

For example, there are many privately-owned companies that do apply a minimum capitalization policy in practice and even have it documented in writing, but often do not have an annual financial statement meeting the definition of an Applicable Financial Statement. For those companies, the government could mitigate its concern about the lack of an Applicable Financial Statement by imposing an aggregate dollar ceiling on the taxpayer’s tax deduction, and that ceiling could be measured by a defined attribute reported on the tax return, such as a percentage of tax gross receipts.

¹ [Selected Issues Relating to Choice of Business Entity, JCX-20-12 \(Mar. 5, 2012\)](#).

For those taxpayers who do have an Applicable Financial Statement, the AICPA recommends that the aggregate dollar ceiling be completely eliminated for several reasons. First, the ceiling imposed by the regulations will present severe compliance challenges to many taxpayers that would defeat the purpose of a de minimis rule. Specifically, larger, more sophisticated businesses that apply a minimum capitalization policy do so for the specific purpose of avoiding complex tracking of numerous small transactions and therefore do not have a single account that tracks these items. Nor do they maintain the detailed records of the items expensed that would enable them to comply with the de minimis rule as currently written. Apart from this concern, the AICPA believes that when a taxpayer is required to abide by an audited financial statement de minimis policy, as the regulations already require, the imposition of the aggregate dollar ceiling is redundant. We believe the government's goal of avoiding income distortion is safely achieved by the Applicable Financial Statement requirement alone, and that this requirement achieves a clear reflection of income without creating the compliance barriers that are raised by the ceiling.

Additional Guidance and Relief is Needed for Accounting Method Changes and to Comply with the Temporary Regulations under Revenue Procedures 2012-19 and 2012-20

Now I'll turn to the transition guidance in Revenue Procedures 2012-19 and 2012-20.

The AICPA commends the IRS and Treasury for permitting automatic accounting method changes to comply with the regulations and for explicitly allowing taxpayers to use statistical sampling procedures. Also, the waiver of the scope limitations for two years will allow taxpayers additional time needed to comply with the regulations.

However, the AICPA believes there are a few areas that should be revised or clarified.

First, and most important, the AICPA recommends that the procedural guidance be amended to permit taxpayers to use extrapolation procedures to compute the section 481(a) adjustments that are required to implement these accounting method changes. Because most of the required accounting method changes will require a section 481(a) adjustment, and many fixed assets subject to the temporary regulations have long tax recovery periods, many taxpayers do not have the information necessary to completely conform to the statistical sampling guidelines for all prior years that may be included the adjustment period. Extrapolation procedures have become an entirely acceptable means of implementing new tax accounting rules. As far back as 1987, for example, with the explicit direction of Congress, the government provided extrapolation procedures in Treas. Reg. § 1.263A-7(c) with respect to the computation of section 481(a) adjustments to implement the uniform capitalization rules.

Second, regarding the de minimis rule, additional transition relief is warranted. Because the temporary regulations were issued late in December 2011, many calendar year taxpayers were not able to comply with the requirement to have a written de minimis policy in place at the beginning of their 2012 tax year. Accordingly, taxpayers should be given some additional time to comply with the written policy requirement.

Finally, the AICPA believes the accounting method procedures should be clarified in a number of respects. One important example is with respect to identifying the situations in which single or multiple Form 3115 filings are required for related changes. Specifically, in one place the revenue procedures indicate that a taxpayer must file a single Form 3115 that includes all concurrent and related accounting method changes, but in other places that a taxpayer may do so. The AICPA recommends that the procedures be clarified to eliminate the inconsistency and clarify that combined filings are permitted, but not required.

Highlights of Forthcoming Submission

In addition to the testimony I've just presented and our letter of April 17th, the AICPA continues to develop additional comments and recommendations on the regulations and related guidance, and expects to submit these in a subsequent letter. Some of the areas that are expected to be addressed include the following:

- The interaction of the various sections of the temporary regulations;
- The types of costs that are included in determining the cost of a material and supply;
- The optional method for rotatable and temporary spare parts;
- The definition of an Applicable Financial Statement;
- The application of the routine maintenance safe harbor;
- The definition of a major component or substantial structural part of a unit of property; and,
- The application of the betterment test in the improvement standards.

Closing

In closing, the AICPA appreciates this opportunity to comment today and we urge the Treasury and the IRS to adopt our recommendations. We also look forward to providing further input and feedback as you work on finalizing the regulations and related guidance.