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Safe Harbor Changes to the Tangible Property Regulations

> **Updates include an increase to the De Minimis safe harbor for taxpayers without audited financial statements and a safe harbor to assist in the handling of refreshes for restaurant and retail companies.**
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> – David McGuire
> Director
> McGuire Sponsel

The IRS updated some of the rules related to the new Tangible Property Regulations. These updates include an increase to the De Minimis safe harbor for taxpayers without audited financial statements, and a safe harbor to assist in the handling of refreshes for restaurant and retail companies. These provide some welcome compliance relief. However, before moving forward it is critical to understand the restrictions and requirements associated with these rules.

Notice 2015-82 increases the De Minimis safe harbor for taxpayers without Applicable Financial Statements (AFS). Under the existing rules taxpayers without an AFS were limited to a De Minimis safe harbor of $500 per item or invoice. Under the new rules this De Minimis safe harbor is increased to $2,500 for tax years beginning on or after 2016.

As part of this Notice the IRS has stated that they will not audit this issue for taxpayers utilizing the higher De Minimis in years prior to 2016 provided they meet the requirements of § 1.263(a)-1(f)(1)(ii). This has led many tax return preparers to ask if they should increase the amount on the 2015 return. This would not be permitted under the new rules due to the restrictions in § 1.263(a)-1(f)(1)(ii). Specifically, to receive the audit protection in prior years the taxpayer must have a capitalization policy in place at the beginning of the tax year in question with the higher De Minimis amount in place.

Due to the requirement of consistency in the capitalization policy it is critical that CPA firms reach out to their clients and put a capitalization policy in place by the end of the year that will utilize the higher threshold starting Jan. 1, 2016.

Rev. Proc. 2015-56 allows applicable restaurant and retail companies to deduct 75 percent of eligible remodels and refreshes. This will open up an opportunity for restaurants and retail clients to expense a large portion of their renovations as a refresh without going through multiple tests to determine what portions would be eligible under the old rules. However, with every benefit comes some restrictions. The IRS has limited the applicability of this rule by putting multiple restrictions on the usage of the safe harbor. In order to determine if a taxpayer wants to utilize this benefit, these restrictions need to be reviewed in detail.

The first restriction is the removal of the ability to take partial dispositions. Under this rule the taxpayer is electing to write off much of the renovation expenses moving forward as "refreshes" and not capital improvements. As a result, the IRS has removed the ability to take a partial disposition for taxpayers that wish to follow this safe harbor. The IRS goes further and requires taxpayers desiring to utilize this

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procedure to file a change in accounting method revoking any prior partial dispositions taken.

The next restriction requires that taxpayers wishing to follow this procedure have an AFS. Similar to the $5,000 De Minimis amount this needs to be a full audit by a licensed CPA firm.

The IRS will also require taxpayers to put the remaining basis of the assets into a General Asset Account. As a reminder General Asset Accounts were an issue under the original iterations of the repair regulations. However, many taxpayers found the accounting for the General Asset Accounts to be cumbersome and restrictive.

Finally, the IRS states that these new regulations do not cover personal property, expansions or renovations that occur during a temporary closing. This will require that taxpayers separate any costs associated with expansions, and personal property before accessing these benefits. Furthermore, if the location closes for more than 21 days to allow for the renovation, this safe harbor does not apply.

Both of these IRS policies provide guidance and opportunities for tax planning with eligible clients. However, it is critical that tax practitioners understand the intricacies of these policies before consulting with their clients. Please feel free to reach out to your McGuire Sponsel representative with any questions.