MS CONSULTANTS, LLC
Cost Segregation Studies & More

June 24, 2013

Ms. Claybon

Thank you for bringing the IRS's view to the AICPA RE Conference today. You win the "prize" for having the liveliest audience of the whole conference.

I was the person in the back who appreciated all the comments regarding cost segregation studies (since that is how I make my living) and also the person who spoke regarding the issue on whether or not a taxpayer needs to capitalize previously expensed items under the new temporary, and soon to be final, regulations.

I have followed the Repair vs. Capitalization subject closely since 2000, when I wrote my first article "Wait, Don't Capitalize That", and have commented to the Treasury Department the first three times the Treasury and the IRS requested commentary on the subject (I am even quoted in the preface to the newest round of temporary regulations). And I respectfully disagree with the IRS's position that taxpayers need to capitalize previously expensed property items for the new regulations.

Up to the issuance of the temporary regulations at the end of 2011, taxpayers had more than a dozen court cases (Fed Ex and Ingram being the best known) where they had guidance from authorities on what the requirements for capitalization should be. And while not being an attorney, and understanding all of the nuances of the law, it seems to me that if someone was correctly following the tax law up through 2011, the temporary regulations issued at the end of 2011 should not cause them to have to change their prior methods and cause them to pick up income for items previously written off. This is the first time in my thirty years of practice that I can remember where the IRS is asking taxpayers to retroactively change what they have done in the past beyond the current tax year - especially if they were correctly following the law that applied at the time of the initial expenditure.

Your argument today is the tradeoff that taxpayers are gaining: The IRS is also going to allow taxpayers to write off items in 2014 that they may have incorrectly capitalized in the past. I respectfully disagree with this argument for most previously capitalized items. My argument is that many of these items you may be referring to were incorrectly capitalized in the past under the old rules, and so therefore most taxpayers are not gaining a significant NEW advantage under this regulation approach. In most cases, they could apply the old law thru 2011, and in many cases have written off the item. For example, a taxpayer s capitalized a newly installed roof in 2002 on the building the taxpayer purchased in 1990. Whether or not this roof should have been capitalized can be determined by following several Court cases (I apologize, I am sitting in Reagan airport while I type this, but I believe the most recent ruling in this area was Brown, but I could be wrong). The new regs do not materially differ from that Court Case ruling, so the taxpayers have not gained any advantage under the new regs in this example.

These new Regulations are changing 30 plus years of tax law, and will be hard for most taxpayers to accept, let alone apply. The burden of asking taxpayers to capitalize items that they previously expensed will lead to confrontations with their CPAs, cause phantom income to be recorded, and only to made worse by telling the taxpayers that if they want to incur additional costs and administrative burdens, they may be able to write off the original (and now retired) structural component as a trade off. This is asking alot of taxpayers.

While I would personally benefit from preparing a lot of cost segregation studies to break down the 9 building systems, I do not believe it is good tax law - fair and understandable. I strongly believe that this portion of the regulations would be easier to apply if the cut-off method was used instead. No prior changes, here is the law going forward. Less administrative burden for both taxpayers and their CPAs, less confrontation over the issue with the IRS (remember, I and many other CPAs still would argue against any of my clients needing to capitalize under the old law), and definitely less administrative burden for the IRS, who in their defense has a lot of issues on their plate for 2013/2014 with the other changes in these regulations (and the thousands of 3115s that will be filed), the new Health Care Act that the IRS will be responsible for marshalling, while all the time working within budget constraints.

Once again, I personally benefit when tax laws are confusing. But I believe in this particular area, simplification is best for everyone. Thank you for taking the time to read through this and giving it consideration.

Very truly yours,

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Roger Upton
Director

Enclosures

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