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OBJECTIVE ADVICE ON THE ROAD OF LIFE

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Dear Client,

We want you to be aware of a couple tax-related items that may have a significant impact on your business tax reporting for the current and upcoming tax years.

The first item is a change in the amount of assets that can be expensed during the tax year under Section 179 of the Internal Revenue Code. As of today, the Code Section 179 limit for tangible personal property (and certain software) for the tax year 2014 is $25,000. This is a significant decrease from the $500,000 limit allowed for 2013 and may have a major impact on your taxable business income for the 2014 tax year. We are hopeful that Congress will increase the limits for 2014 and will notify you if they pass a retroactive increase for Code Section 179 expensing.

The next item is a change in the way certain expenses are reported AND MAY REQUIRE A POLICY CHANGE TO BE IMPLEMENTED (retroactively) as of January 1, 2014. Businesses that do not make this policy change may be severely limited regarding their ability to expense certain types of items. This change is necessary due to IRS regulations released in September of 2013 regarding the capitalization of tangible property costs. These regulations are lengthy and complex and must be followed for tax years beginning after December 31, 2013 (whether a calendar year or a fiscal year) such as a fiscal year beginning July 1, 2014.

There are five categories of items affected by these new IRS regulations:

1) Materials and supplies,
2) Repairs and maintenance,
3) Capital expenditures,
4) Disbursements to acquire or produce tangible property, and
5) Disbursements to improve tangible property

The regulations set forth the general rule that amounts paid to improve a unit of property must be capitalized. On the other hand, the regulations allow a current deduction for repairs and maintenance to property. One key concept in the regulations is the “unit of property” (UOP) that is being improved or repaired. The smaller the UOP, the more likely it is that costs incurred in connection with it will have to be capitalized.

The good news is that the final regulations allow the de minimis safe harbor election which allows eligible businesses to immediately expense certain property that would otherwise have to be capitalized. Any business that has certain nontax accounting procedures in place at the beginning of the year will qualify for this safe harbor election. Those certain nontax accounting procedures must specify that the business will expense amounts paid for property costing less than a specified dollar amount OR that have a useful life of twelve months or less (i.e. a capitalization policy). If you already have a capitalization policy in place, it may need to be updated to meet the new IRS regulations.

The ***amount*** that can be expensed under this safe harbor election depends upon whether the business has an Applicable Financial Statement (AFS). These statements include certified audited financial statements used for credit purposes, reporting to owners, or other substantial nontax purposes as well as financial statements filed with the SEC or provided to a federal or state government or agency (other than the SEC or IRS).

Those businesses ***with*** an AFS must have written accounting procedures in place by January 1, 2014 (for calendar year businesses). Those that have made the election can expense property that costs up to $5,000 (per item), if, in accordance with their written accounting procedures, the property is expensed on their AFS.

Those businesses ***without*** an AFS must also have accounting procedures in place by January 1, 2014 (for calendar year businesses). They can then expense property costing up to $500 (per item), if, in accordance with those procedures, the property is expensed in their books and records.

We are providing the sample Accounting Capitalization Policies for your use (see attached). Please prepare the one that applies to your business. ***Upon completion please forward a copy of your policy to our office.*** We will keep the policy in our permanent file. If you are uncertain as to which policy to adopt, please call us for guidance.

In regards to larger expenditures, another safe harbor election is available to qualifying small taxpayers – those with average annual gross receipts of $10 million or less in the three preceding tax years – to deduct improvements made to certain buildings. This election would be made by including a statement with the tax return for the year the costs are incurred for the building. We can help you to take advantage of this rule by filing the necessary election statement.

We hope this information is helpful. If you would like more details, please don't hesitate to give us a call.

Very truly yours,

Roback, Kumlander & Pehl

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