ICS TAX, LLC

Accounting Methods Guidance

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ICS Tax, LLC

ABOUT US

- ICS Tax, LLC (ICS) is a national consulting firm providing innovative tax planning strategies to taxpayers and their tax professionals to identify credits and incentives that reduce tax liabilities and increase profitability
- We combine top talent and a multidisciplinary approach to assist with Comprehensive Fixed Asset Reviews, Energy Efficiency Incentives (179D/45L), Research & Development Tax Credits, Cost Segregation Studies, IC-DISC Export Incentives, Accounting Methods, and Utility Rebates.

YOUR PRESENTER

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AMERICAN SOCIETY OF COST SEGREGATION PROFESSIONALS

- Alex Bagne is the President of ICS Tax, LLC (ICS). His expertise includes the tangible property regulations, cost segregation, energy efficiency incentives (179D/45L), R&D credits, fixed asset reviews, and IC-DISC export incentives. Prior to ICS, Alex worked for a decade with several Big Four firms.
- Alex earned an BSBA in accounting from The Ohio State University, an MBA from the University of Minnesota, and a JD from the Tulane University Law School in New Orleans, Louisiana.
- Alex is a licensed attorney, a CPA, and a past president and Certified Member of the American Society of Cost Segregation Professionals.

PRESENTATION OVERVIEW

- Taxpayers and tax professionals use accounting method changes as a powerful mechanism to implement valuable tax strategies as well as to maintain compliance or remove IRS audit exposure.
- Upon completion of the course, you'll be able to:
  - Understand several popular accounting method changes
  - Calculate the §481(a) adjustment required by changes in accounting methods
  - Complete and file Form 3115, Application for Change in Accounting Method
  - Discuss recent tax rule changes and how they apply to accounting methods

THE WHAT: ACCOUNTING METHOD CHANGES

DEFINITION: ACCOUNTING METHOD

- An accounting method is the method by which income and expenses are reported for taxation purposes.
- A change in accounting method includes any change in the taxpayer's overall method of accounting, e.g., cash to accrual, but it also includes changes in the treatment of any "material" item.
- The IRS requires taxpayers to choose an accounting method that accurately reflects their income and to be consistent in their choice of accounting method from year to year.

TWO TYPES: AUTOMATIC VS. NON-AUTOMATIC

- Automatic:
  - An applicant that timely files and complies with the automatic change procedures is granted consent to change its accounting method.
  - Method subject to review by the IRS.
  - No user fee is required.

TWO TYPES: AUTOMATIC VS. NON-AUTOMATIC, CONT'D

- Non-Automatic (advanced consent):
  - Requires approval by the IRS National Office.
  - If approved, the filer will receive a letter ruling on the requested change.
  - Significant User Fees: $10,800 to request a non-automatic change in method of accounting per Rev. Proc. 2021-1.

DESIGNATED CHANGE NUMBER (DCN)

- Each Automatic Method Change has a Designated Change Number (DCN).
- About 200 DCNs.

List of DCNs	
No.	**Change**
1	**Commodity Credit Corporation loans (section 77)**—for loans received from the Commodity Credit Corporation, **from** including the loan amount in gross income for the tax year in which the loan is received **to** treating the loan amount as a loan. See section 2.01 of Rev. Proc. 2015-14. **Note.** This change is implemented on a cut-off basis.
2	**Advances made by a lawyer on behalf of clients (section 162)**—**from** treating advances of money to or on behalf of their clients for litigation or other client expenses as deductible expenses **to** treating those advances as a loan. See section 3.01 of Rev. Proc. 2015-14.
3	**ISO 9000 costs (section 162)**—**to** treating the costs as deductible, except to the extent they result in the creation or acquisition of an asset having a useful life substantially beyond the tax year. See section 3.02 of Rev. Proc. 2015-14.
4	**Restaurant smallwares costs (section 162)**—**to** the smallwares method described in Rev. Proc. 2002-12, 2002-1 C.B. 374 (that is, as materials and supplies that are not incidental under Regulations section 1.162-3). See section 3.03 of Rev. Proc. 2015-14.
5	**Bad debts (section 166)**—for an applicant other than a bank, **from** accounting for bad debts using a reserve or other improper method **to** a specific charge-off method that complies with section 166. See section 4.01 of Rev. Proc. 2015-14.
6	**Bad debt conformity for banks (section 166)**—for banks other than new banks, **to** the method that conforms to Regulations section 1.166-2(d)(3) for the first time the bank makes this change, or **to** involuntarily revoke this method. This change does not fall under the procedures of Rev. Proc. 2015-14. Instead, see Regulations section 1.166-2(d)(3). **Note.** This change is implemented on a cut-off basis and generally with audit protection, but with some conditions or limitations.
7	**Depreciation or amortization (impermissible to permissible) (sections 56, 167, 168, 197, 280F, 1400I, 1400L, 1400N, and former section 168)**—**from** an impermissible method **to** a permissible method for changes allowed under Regulations section 1.446-1(e)(2)(ii)*(d)*, and for depreciable property owned at the beginning of the year of change. Complete Schedule E of Form 3115. An applicant changing its method of accounting for depreciation because of a change described in designated automatic accounting method change number 10 (sale or lease transactions) must file Form 3115 according to the designated change number 10. Additionally, a qualified small taxpayer qualifies for a reduced Form 3115 filing requirement. See section 6.01 of Rev. Proc. 2015-14.
8	**Depreciation (permissible to permissible) (sections 56 and 167)**—**from** a permissible method **to** another permissible method listed in section 6.02 of Rev. Proc. 2015-14. Complete Schedule E of Form 3115. Change is implemented on a modified cut-off basis. An applicant making a change from a permissible to another permissible method of depreciating MACRS property must file Form 3115 according to designated change number 200. Additionally, a qualified small taxpayer qualifies for a reduced Form 3115 filing requirement. See section 6.02 of Rev. Proc. 2015-14.
10	**Sale, lease, or financing transactions (sections 61, 162, 167, 168, and 1012)**—**from** improperly treating property as sold, leased or, financed **to** a permissible method as described in section 6.03 of Rev. Proc. 2015-14. See section 6.03 of Rev. Proc. 2015-14. **Note.** This change is implemented on a cut-off basis and does not receive audit protection.

THE WHY: ACCOUNTING METHOD CHANGES

WHY MAKE AN ACCOUNTING METHOD CHANGE?

- As a tax planning tool, accounting methods help taxpayers implement cost segregation studies and energy efficiency incentives, adopt favorable provisions of the Tangible Property Regulations, and numerous other tax minimization strategies.
- Accounting methods also help taxpayers correct improper methods to maintain tax compliance or to eliminate audit risk.

POPULAR METHOD CHANGES: DEPRECIATION/COST SEGREGATION

- Residential rental property is depreciated over a lengthy 27.5 years whereas commercial real estate is depreciated even longer over 39 years.
- IRS rules allow non-building components such as personal property and land improvements to be segregated from the building and depreciated more rapidly, generally over 5, 7, and 15 years.
- DCN 7 allows taxpayers to retroactively make depreciation changes.

POPULAR METHOD CHANGES: DEPRECIATION/COST SEGREGATION

- Examples:
  - Reclassifying process-related electrical, plumbing, fire protection, and HVAC systems in manufacturing center.
  - Reclassifying decorative lighting, millwork, cabinetry, carpeting, and wallcovering in office building or hotel.
  - Qualified Leasehold Improvements depreciated over 39 years rather than 15.
  - Missed bonus depreciation.

POPULAR METHOD CHANGES: QUALIFIED IMPROVEMENT PROPERTY (QIP)

- Starting in 2018, the TCJA consolidated four special asset categories (Qualified Improvement Property (QIP), Qualified Leasehold Improvement Property, Qualified Retail Improvement Property and Qualified Restaurant Improvement Property) into just one category called QIP.
- Our legislators intended to change QIP to a 15-year recovery period making it eligible for 100% bonus depreciation, but that change was not included in the TCJA and these items were depreciable over a lengthy 39 years.
- The CARES Act **retroactively** changed QIP to 15-year property, thus making it eligible for bonus depreciation.

THE DEFINITION OF QIP

- Improvement must be **made by the taxpayer**.
- Improvement to **interior** portion of a building which is **nonresidential**.
- Improvement placed in service **after** the date the building was first placed in service.
- Improvement must be **Sec. 1250 Property**.
- **Excludes** expenses attributable to the **enlargement** of the building, **elevators**, **escalators**, or **internal structural framework** of the building.

REV. PROC. 2020-25/DCN 244

- Rev. Proc. 2020-25 provides guidance on DCN 244.
- Applies to QIP placed in service after December 31, 2017, for the 2018, 2019 or 2020 tax year.
- Not affected by other accounting method changes (e.g., DCN 7).
- Reduced filing requirements.
- Rev. Proc. 2020-25 also allows a taxpayer to make a late election or to revoke or withdraw an election for the 2018, 2019 or 2020 tax year (e.g., elect out of 100% bonus, use 50% bonus, use ADS).

POPULAR METHOD CHANGES: REPAIR AND MAINTENANCE COSTS

- The new Tangible Property Regulations allow taxpayers to retroactively review expenditures that were capitalized but qualify as repair and maintenance expenses, such as replacing roof membranes, resealing parking lots, and replacing of HVAC components.
- DCN 184 allows taxpayers to take an immediate deduction on such costs rather than depreciate them over a lengthy period.

POPULAR METHOD CHANGES: REPAIR AND MAINTENANCE COSTS

- Examples (as provided by the Tangible Property Regulations):
  - Replacement of entire roof constitutes a restoration and requires capitalization, replacement of roof membrane does not.
  - Replacement of 1 of 3 furnaces of buildings HVAC system does not result in a restoration and can be immediately expensed.
  - Replacement of 3 of 10 roof mounted heating and air conditioning units does not constitute a restoration and can be immediately expensed.

POPULAR METHOD CHANGES: REPAIR AND MAINTENANCE COSTS

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  - Replacement of 1 of 3 furnaces of buildings HVAC system does not result in a restoration and can be immediately expensed.
  - Replacement of 3 of 10 roof mounted heating and air conditioning units does not constitute a restoration and can be immediately expensed.

POPULAR METHOD CHANGES: REPAIR AND MAINTENANCE COSTS

- Examples, continued:
  - Replacement of 30% of electrical system wiring does not result in restoration and can be expensed.
  - Replacement of 8 of 20 sinks does not result in a restoration.
  - Replacement of 100 of 300 exterior windows does not result in a restoration; replacement of 200 of 300 exterior windows does result in a restoration.

POPULAR METHOD CHANGES: §179D ENERGY EFFICIENT COMMERCIAL BUILDING DEDUCTION

- Taxpayers who construct new buildings or make improvements to existing ones can take an immediate deduction of up to $1.80/SF for investments in efficient lighting systems, HVAC and hot water systems, and the building envelope.
- For most taxpayers, this is vastly more preferential than depreciating these expenditures as real property over a lengthy 27.5- or 39-year period.
- DCN 152 allows taxpayers to retroactively deduct these costs.

POPULAR METHOD CHANGES: §179D ENERGY EFFICIENT COMMERCIAL BUILDING DEDUCTION

- Examples:
  - Taxpayer replaced lighting systems in 100,000 SF hotel, building already had energy efficient HVAC system. Building qualified for $1.80/SF §179D Deduction and generate $180,000 in additional deductions.
  - HOWEVER, if contractor installs energy efficient lights for a public agency such that the contractor is eligible to take the §179D Deduction, contractor can only amend – method change not allowed.

POPULAR METHOD CHANGES: DISPOSITIONS OF TANGIBLE ASSETS

- Taxpayers often have "ghost" assets on their fixed asset schedules, such as old tenant improvements or machinery and equipment.
- DCNs 205 and 206 allow taxpayers to take abandonment losses on these assets.

POPULAR METHOD CHANGES: DISPOSITIONS OF TANGIBLE ASSETS

- Other benefits of disposing of ghost assets.
  - Simplifies Record Keeping/Fixed Asset Tracking
  - Eliminates Depreciation Recapture (i.e., IRS. collects income tax on a gain realized by a taxpayer when the taxpayer disposes of an asset that had previously provided an offset to ordinary income for the taxpayer through depreciation).
  - May Reduce Various Property Taxes.

POPULAR METHOD CHANGES: CASH METHOD VS. ACCRUAL METHOD

- Cash Method provides simplicity and greater control over when income and expense is recognized but the Accrual Method may be mandatory.
- Multiple DCN options (32, 33, 34, 122, 123, 126, 127, 128) depending on situation. See List of Automatic Changes in the 3115 instructions.
- New DCN 233 Expands the number of small business taxpayers (i.e., average annual gross receipts of $25M or less) eligible to use a cash method of accounting. These businesses are exempt from certain accounting rules for inventories, cost capitalization, and long-term contracts (Rev. Proc. 2018-40).

CHANGES THAT ARE NOT ACCOUNTING METHOD CHANGES

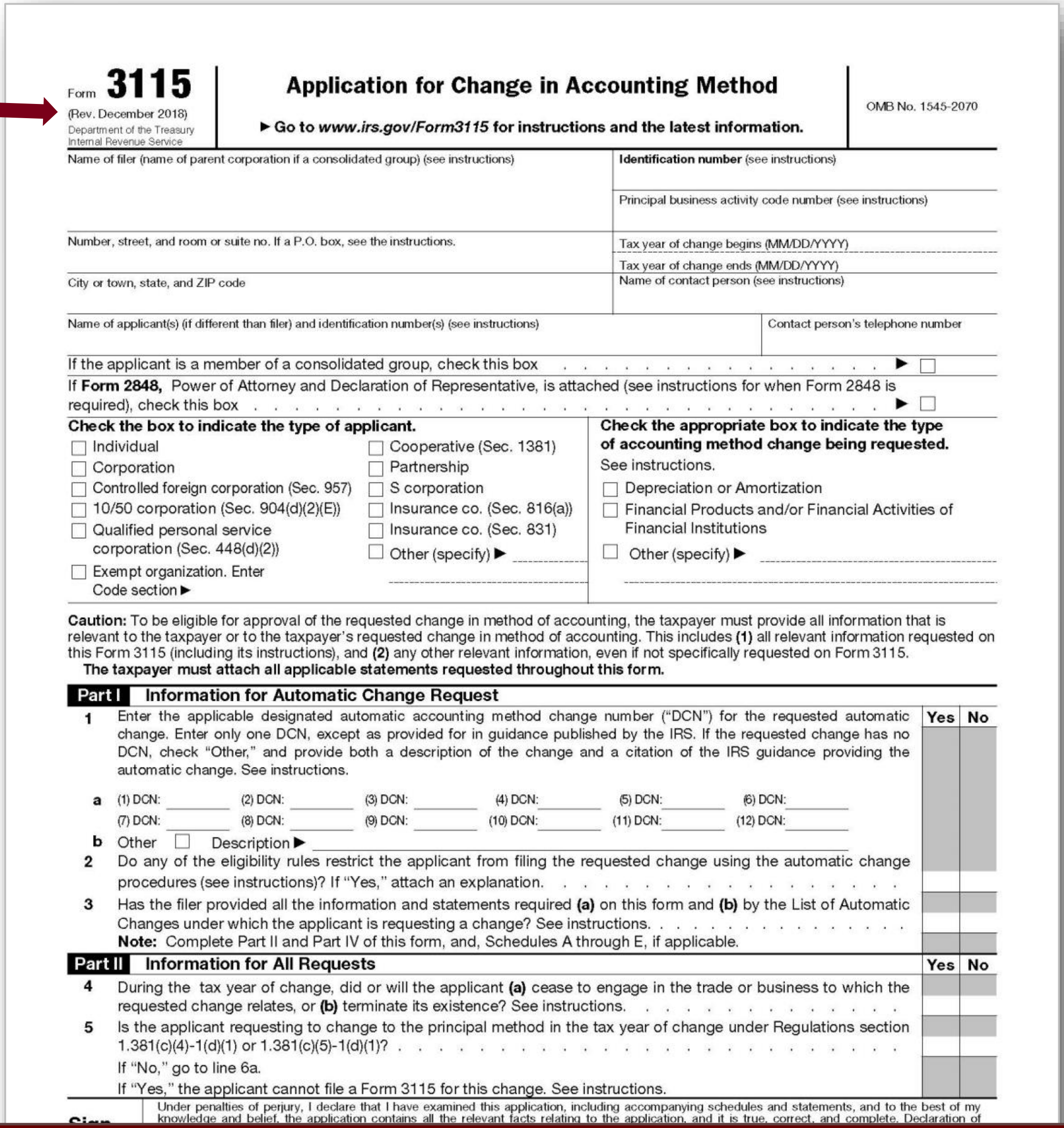
- Taxpayers can make several changes on a go-forward basis that are not accounting method changes. Examples include:
  - Correction of Computational or Posting Errors.
  - A change in an income or deduction amount that does not involve the proper time for recognizing income or expense (e.g., omitting rental income).
  - Elections: (e.g., De Minimis Safe Harbor, §179 Deduction). Requires an annual election statement to be filed with tax return.
  - Implementing a cost segregation study where the taxpayer has yet to establish a previous method (e.g., the building was placed in service in 2018, taxpayer has yet to file 2018 return).

THE HOW: ACCOUNTING METHOD CHANGES

Last Update Dec. 2018

FORM 3115

- Taxpayers wanting to make an accounting method change file Form 3115, Application for Change in Accounting Method.
- Form 3115 has 8 pages, but not all are used at once.



Form **3115** (Rev. December 2018) Department of the Treasury Internal Revenue Service

Application for Change in Accounting Method

▶ Go to *www.irs.gov/Form3115* for instructions and the latest information.

OMB No. 1545-2070

Name of filer (name of parent corporation if a consolidated group) (see instructions)	**Identification number** (see instructions)
	Principal business activity code number (see instructions)
Number, street, and room or suite no. If a P.O. box, see the instructions.	Tax year of change begins (MM/DD/YYYY)
	Tax year of change ends (MM/DD/YYYY)
City or town, state, and ZIP code	Name of contact person (see instructions)
Name of applicant(s) (if different than filer) and identification number(s) (see instructions)	Contact person's telephone number

If the applicant is a member of a consolidated group, check this box ▶ ☐

If **Form 2848,** Power of Attorney and Declaration of Representative, is attached (see instructions for when Form 2848 is required), check this box ▶ ☐

Check the box to indicate the type of applicant.

☐ Individual
☐ Corporation
☐ Controlled foreign corporation (Sec. 957)
☐ 10/50 corporation (Sec. 904(d)(2)(E))
☐ Qualified personal service corporation (Sec. 448(d)(2))
☐ Exempt organization. Enter Code section ▶
☐ Cooperative (Sec. 1381)
☐ Partnership
☐ S corporation
☐ Insurance co. (Sec. 816(a))
☐ Insurance co. (Sec. 831)
☐ Other (specify) ▶

Check the appropriate box to indicate the type of accounting method change being requested. See instructions.

☐ Depreciation or Amortization
☐ Financial Products and/or Financial Activities of Financial Institutions
☐ Other (specify) ▶

Caution: To be eligible for approval of the requested change in method of accounting, the taxpayer must provide all information that is relevant to the taxpayer or to the taxpayer's requested change in method of accounting. This includes **(1)** all relevant information requested on this Form 3115 (including its instructions), and **(2)** any other relevant information, even if not specifically requested on Form 3115.

The taxpayer must attach all applicable statements requested throughout this form.

Part I Information for Automatic Change Request — **Yes No**

1 Enter the applicable designated automatic accounting method change number ("DCN") for the requested automatic change. Enter only one DCN, except as provided for in guidance published by the IRS. If the requested change has no DCN, check "Other," and provide both a description of the change and a citation of the IRS guidance providing the automatic change. See instructions.

a (1) DCN: (2) DCN: (3) DCN: (4) DCN: (5) DCN: (6) DCN:
(7) DCN: (8) DCN: (9) DCN: (10) DCN: (11) DCN: (12) DCN:

b Other ☐ Description ▶

2 Do any of the eligibility rules restrict the applicant from filing the requested change using the automatic change procedures (see instructions)? If "Yes," attach an explanation.

3 Has the filer provided all the information and statements required **(a)** on this form and **(b)** by the List of Automatic Changes under which the applicant is requesting a change? See instructions.
Note: Complete Part II and Part IV of this form, and, Schedules A through E, if applicable.

Part II Information for All Requests — **Yes No**

4 During the tax year of change, did or will the applicant **(a)** cease to engage in the trade or business to which the requested change relates, or **(b)** terminate its existence? See instructions.

5 Is the applicant requesting to change to the principal method in the tax year of change under Regulations section 1.381(c)(4)-1(d)(1) or 1.381(c)(5)-1(d)(1)?
If "No," go to line 6a.
If "Yes," the applicant cannot file a Form 3115 for this change. See instructions.

Under penalties of perjury, I declare that I have examined this application, including accompanying schedules and statements, and to the best of my knowledge and belief, the application contains all the relevant facts relating to the application, and it is true, correct, and complete. Declaration of

INSTRUCTIONS TO FORM 3115

- The 29 pages of instructions are reasonable intuitive.
- However, they are not always updated (update was Dec. 2018)

Instructions for Form 3115

(Rev. December 2018)

Department of the Treasury
Internal Revenue Service

Application for Change in Accounting Method

Section references are to the Internal Revenue Code unless otherwise noted.

CAUTION *All references to Rev. Proc. 2015-13 are to Rev. Proc. 2015-13, 2015-5 I.R.B. 419 (as clarified and modified by Rev. Proc. 2015-33, 2015-24 I.R.B. 1067, and as modified by Rev. Proc. 2017-59, 2017-48 I.R.B. 543, and by section 17.02 of Rev. Proc. 2016-1, 2016-1 I.R.B. 1), or any successor.*

All references to Rev. Proc. 2018-31 and the List of Automatic Changes are to Rev. Proc. 2018-31, 2018-22 I.R.B. 637 (as modified by Rev. Proc. 2018-60, 2018-51 I.R.B. 1045, Rev. Proc. 2018-56, 2018-50 I.R.B. 985, Rev. Proc. 2018-49, 2018-41 I.R.B. 548, Rev. Proc. 2018-44, 2018-37 I.R.B. 426, Rev. Proc. 2018-40, 2018–34 I.R.B. 320, Rev. Proc. 2018-35, 2018-28 I.R.B. 204, and Rev. Proc. 2018-29, 2018-22 I.R.B. 634), or any successor.

All references to Rev. Proc. 2019-1 are to Rev. Proc. 2019-1, 2019-1 I.R.B. 1, or any successor (updated annually).

Future Developments

For the latest information about developments related to Form 3115 and its instructions, such as legislation enacted after they were published, go to *IRS.gov/Form3115*.

What's New

Small business taxpayers. Effective for tax years beginning after 2017, the Tax Cuts and Jobs Act (P.L. 115-97) expanded the eligibility of small business taxpayers to use the cash method of accounting. The cash method is available for taxpayers that had average annual gross receipts for the 3 preceding tax years of $25 million or less. See the instructions for Schedule A, later. Qualifying small business taxpayers are also exempt from the following accounting rules.

- The requirement to keep inventories. See section 471(c) and the instructions for Schedule A.
- The uniform capitalization rules. See section 263A(i) and the instructions for Schedule D.
- The requirement to use the percentage-of-completion method for construction contracts, expected to be completed within two years. See section 460(e) and the instructions for Schedule D.

Advance payments. See the instructions for Schedule B for changes to the election to defer advance payments.

Terminating S corporations. Special rules apply for eligible terminated S corporations (as defined in section 481(d)(2)) that change their method of accounting from cash to accrual. See the instructions for Part IV.

General Instructions

Method Change Procedures

CAUTION *When filing Form 3115, you must determine if the IRS has issued any new published guidance which includes revenue procedures, revenue rulings, notices, regulations, or other relevant guidance in the Internal Revenue Bulletin. For the latest information, visit IRS.gov.*

For general application procedures on requesting accounting method changes, see Rev. Proc. 2015-13. Rev. Proc. 2015-13 provides procedures for both automatic and non-automatic changes in method of accounting.

Automatic change procedures. Unless otherwise provided in published guidance, you **must** file under the automatic change procedures if you are eligible to request consent to make a change in your method of accounting under the automatic change procedures for the requested year of change. See the instructions for Part I later, and the List of Automatic Changes in Rev. Proc. 2018-31.

A Form 3115 filed under these procedures may be reviewed by the IRS. If it is, you will be notified if information in addition to that requested on Form 3115 is required or if your request is denied. No user fee is required. An applicant that timely files and complies with the automatic change procedures is granted consent to change its accounting method, subject to review by the IRS National Office and operating division director.

Ordinarily, you are required to file a separate Form 3115 for each change in method of accounting. However, in some cases you are required or permitted to file a single Form 3115 for particular concurrent changes in method of accounting. See section 6.03(1)(b) of Rev. Proc. 2015-13 for more information.

Note. The List of DCNs (Designated automatic accounting method change number) at the end of these instructions is a list of many accounting method changes and is presented for informational purposes only and subject to the most recently issued Revenue Procedures.

Reduced Form 3115 filing requirement. A qualified small taxpayer qualifies for a reduced Form 3115 filing requirement for the following DCNs: 7, 8, 21, 87, 88, 89, 107, 121, 145, 157, 184–193, 198, 199, 200, 205, 206, 207, and 222. A qualified small taxpayer is a taxpayer with average annual gross receipts of less than or equal to $10 million for the 3 tax years preceding the year of change. See *Year of Change*, later. A reduced Form 3115 filing requirement involves completing only certain lines and schedules of the Form 3115. For qualifying changes and filing requirements, see the List of Automatic Changes.

Non-automatic change procedures. If you do not qualify to file under the automatic change procedures for the requested change in method of accounting for the requested year of change, you may be able to file under the non-automatic change

PROCEDURAL RULES

- Instructions for specific accounting method changes are often in various Revenue Procedures that are continuously superseded and replaced.
- The latest general procedures are in Rev. Proc. 2015-13.
- The latest list of automatic changes and specific instructions for each one are in Rev. Proc. 2019-43, but there have been numerous other Rev. Procs that modify it.

26 CFR 601.204: Changes in accounting periods and in methods of accounting.
(Also Part I, §§ 56, 61, 77, 118, 162, 163, 166, 167, 168, 171, 174, 179D, 194, 195, 197, 248, 263, 263A, 267, 280F, 404, 446, 447, 448, 451, 454, 455, 460, 461, 467, 471, 472, 475, 481, 585, 709, 807, 816, 832, 833, 846, 860A-860G, 861, 904, 953, 985, 1272, 1273, 1278, 1281, 1363, 1400I, 1400L, 1400N; 1.61-1, 1.61-4, 1.61-8, 1.77-1, 1.77-2, 1.118-2, 1.162-1, 1.162-3, 1.162-4, 1.162-11, 1.162-12, 1.166-1, 1.166-2, 1.166-4, 1.167(a)-2, 1.167(a)-3(b), 1.167(a)-4, 1.167(a)-7, 1.167(a)-8, 1.167(a)-11, 1.167(a)-14, 1.167(e)-1, 1.168(d)-1, 1.168(i)-1, 1.168(i)-4, 1.168(i)-6, 1.168(i)-7, 1.168(i)-8, 1.168(k)-1, 1.171-4, 1.174-1, 1.174-3, 1.174-4, 1.179-5, 1.194-1, 1.195-1, 1.197-2, 1.248-1, 1.263(a)-1, 1.263(a)-2, 1.263(a)-3, 1.263(a)-4, 1.263(a)-5, 1.263A-1, 1.263A-2, 1.263A-3, 1.263A-4, 1.263A-7, 1.267(a)-1, 1.280F-6, 1.404(b)-1T, 1.446-1, 1.446-1T, 1.446-2, 1.446-5, 1.446-6, 1.446-7, 1.448-1T, 1.448-2, 1.451-1, 1.451-3, 1.451-8, 1.454-1, 1.455-6, 1.460-4, 1.461-1, 1.461-4, 1.461-5, 1.467-1, 1.471-1, 1.471-2, 1.471-3, 1.471-4, 1.471-5, 1.471-8, 1.472-1, 1.472-2, 1.472-6, 1.472-8, 1.481-1, 1.481-4, 1.709-1, 1.709-2, 1.832-4, 1.832-5, 1.860A-6, 1.861-18, 1.985-5, 1.985-8, 1.1016-3, 1.1245-3, 1.1272-1, 1.1273-1, 1.1273-2, 1.1363-2, 1.1374-4, 1.1400L(b)-1.)

Rev. Proc. 2019-43

ATTACHMENT TO FORM 3115

- In addition to filing Form 3115, the taxpayer may need to provide an attachment that lists additional detail.

Filer: TAXPAYER NAME
EIN: XX-XXXXXXX
Attachment to Form 3115
Tax Year Ended December 31, 2016

Applicant	EIN	Principal Business Activity Code
TAXPAYER NAME	XX-XXXXXXX	XXXXXX

Part II, Question 7b

The Applicant is not under examination. No further statement is required.

Part II, Question 14

a. The Applicant is requesting permission to change its method of accounting for qualifying energy-efficient property within the meaning of §179D.
b. The Applicant's present method of accounting for qualifying energy-efficient property described in Line 12(a) is to recover amounts capitalized under section 168 and related regulations.
c. The Applicant's proposed method of accounting for qualifying energy-efficient property described in Line 12(a) is to deduct eligible amounts under §179D and to properly reflect such deduction as a reduction in the basis of such assets.
d. The Applicant uses the accrual method of accounting.

Part II, Question 15a

The Applicant's trade or business is owning and leasing nonresidential commercial real estate.

Part II, Question 16

The Applicant constructed [Building Name], a [BUILDING DESCRIPTION] located in [CITY, STATE]. [ENTER OTHER BUILDING DETAILS, SUCH AS OCCUPANCY DATE, LEED CERTIFICATION, ENERGY EFFICIENT FEATURES, ETC.].

The Applicant is currently depreciating these improvements as buildings over 39 years using the straight-line method. The Applicant wants to change its method of accounting to deduct under §179D amounts paid or incurred for the installation of energy efficient commercial building property as defined in §179D(c)(1).

A taxpayer making this change must attach a certification as required by section 4 of Notice 2006-52, 2006-1 C.B. 1175, or section 5 of Notice 2008-40, 2008-14 I.R.B. 725, to demonstrate the energy efficient commercial building property has achieved the reduction in energy and power costs or in lighting power density necessary to qualify for the §179D deduction. These certifications are attached.

Part II, Question 17

The change of accounting method will not be used for the Applicant's books, records and financial statements because the change of accounting method is not required or permitted under generally accepted accounting principles (GAAP).

TOP TIP…

- While Form 3115, the corresponding instructions, and the related Revenue Procedures and other rules are lengthy, tax preparers only need to know a small portion for any given change.
- The key is to determine which sections are relevant.

COMPLETING FORM 3115

- Not all parts and schedules from Form 3115 are used and should be left blank.

Table B: Schedules to Complete on Form 3115 for Common Accounting Method Changes

Information to be completed for common method change requests

Common Method Changes	Schedule A		Schedule B	Schedule C		Schedule D			Schedule E
	Part I	Part II		Part I	Part II	Part I	Part II	Part III	
Accrual to Cash	X	X							
Cash to Accrual	X								
Capitalize to Expense									
Expense to Capitalize								X*	X*
Depreciation									X
Long-Term Contracts						X		X	
Inventory Valuation Change							X	X*	
LIFO Change–Including Pooling				X	X				
Change to Deferral Method for Advanced Payments			X						

Table A: Parts to Complete on Form 3115 for Accounting Method Changes

Information to be completed for automatic and non-automatic change requests

	Part I	Part II	Part III	Part IV
Automatic Change	X	X		X
Non-Automatic Change		X	X	X

COMPLETING FORM 3115, CONT'D

- Most information on Page 1 top is found on the taxpayer's income tax return.
- **Part I** is for Automatic Changes, whereby the taxpayer lists the DCN, which can be found in the instructions.
- **Part II** information is required for all accounting methods. My defaults are check "No" for 6a, 8a, and 10 – 17, "Yes" for 7a and 18, "Not under exam" for 7b, and the rest blank. However, each question should be reviewed thoroughly.

COMPLETING FORM 3115, CONT'D

- Part IV: The 481(a) Adjustment
  - Section 481(a) provides that, where a taxpayer's taxable income for a tax year is computed under a method of accounting different from that previously used, an adjustment will be made to prevent amounts from being duplicated or omitted solely by reason of the change in accounting method.

SAMPLE 481(a) CALC: DEPRECIATION

- Taxpayer purchased a building in 2017 for $3.9M and has been depreciating it as real property over 39 years. As a result of a cost segregation study completed in 2021, the taxpayer carved out $780,000 as 5-year property.
- The 481(a) Adjustment would be $(565,216), the difference between the original and proposed accumulated depreciation at year-end 2020. For 2021, the taxpayer would take $169,856 of depreciation expense.

	Building Tax Basis:		Segregated Tax Basis:			
	$ 3,900,000		$ 780,000	$ 3,120,000		
	Original Method		Proposed Method			
	Annual Depr. Exp.	Accumulated	Annual Depr. Exp.		Accumulated	481(a)
Year	39-Year	Depreciation	5-Year	39-Year	Depreciation	Adjustment
2017	$ 100,000	$ 100,000	$ 156,000	$ 80,000	$ 236,000	
2018	$ 100,000	$ 200,000	$ 249,600	$ 80,000	$ 565,600	
2019	$ 100,000	$ 300,000	$ 149,760	$ 80,000	$ 795,360	
2020	$ 100,000	$ 400,000	$ 89,856	$ 80,000	$ 965,216	$ (565,216)
2021	$ 100,000	$ 500,000	$ 89,856	$ 80,000	$ 1,135,072	
2022	$ 100,000	$ 600,000	$ 44,928	$ 80,000	$ 1,260,000	

SAMPLE 481(a) CALC: CASH TO ACCRUAL METHOD OF ACCOUNTING

- ABC Corporation, a calendar year taxpayer using the cash method of accounting, has the following items of unreported income and expense on December 31, 2020:

Accrued income	$250,000
Uncollectible amounts based on the nonaccrual-experience method	$50,000
Accrued amounts properly deductible (economic performance has occurred)	$75,000
Expenses eligible for recurring item exception	$5,000

- ABC Corporation changes to an overall accrual method, a nonaccrual-experience method, and the recurring item exception for calendar year 2021. The section 481(a) adjustment is calculated as of January 1, 2021, as follows:

Accrued income (Line 2a)	$250,000	
Less:		
Uncollectible amount	(50,000)	
Net income accrued but not received		$200,000
Less:		
Accrued expenses (Line 2c)	(75,000)	
Expenses deducted as recurring item (Line 2g)	(5,000)	
Total expenses accrued but not paid		(80,000)
Section 481(a) adjustment		**$120,000**

REPORTING THE 481(a) ADJUSTMENT

- Form 1120
  - If the net section 481(a) adjustment is positive, report it on Form 1120, line 10, as other income. If the net section 481(a) adjustment is negative, report it on line 26 as a deduction.
- Form 1120-S
  - Positive 481(a) is taken on Line 5. Other Income (Loss). Negative 481(a) is taken on Line 19. Other Deductions.
- Form 1065
  - Include any net positive section 481(a) adjustment on page 1 of Form 1065, line 7. If the net section 481(a) adjustment is negative, report it on page 1, line 20.

AUDIT PROTECTION FOR YEARS PRIOR TO THE CHANGE

If a taxpayer files a timely Form 3115 pursuant to Rev. Proc. 2015-13, the IRS generally will not require the taxpayer to change its method of accounting for the same item for any taxable year prior to the year of change. The IRS may, however, make a method change for a prior year in any of the following circumstances:

- The change is not made or is made improperly;
- The requested change is to a sub-method and the IRS's change is to the method itself;
- The IRS's change is a prior year IRS-initiated change; or
- There is a pending or future criminal investigation or proceeding concerning the taxpayer's tax liability, or the possibility of false or fraudulent statements by the taxpayer relating to its tax liability, for the prior year.

SOME THINGS TO KNOW…

- Some method changes can and should be filed on one Form 3115s, such as DCN 7 for Depreciation and DCN 205 for Missed Retirements.
- Taxpayers generally cannot amend a return to include a new accounting method change. If a taxpayer files a return and wants to make an accounting method change, they can file a "superseding" tax return before the extended due date.
- There are rules prohibiting making the same method change twice within a certain period. Sometimes these rules are temporarily waived, such as DCN 184 for Repairs and Maintenance Expenditures under the TPRs.

THE WHEN AND THE WHERE: ACCOUNTING METHOD CHANGES

WHEN AND WHERE TO FILE

- The original Form 3115 should be filed with the income tax return.
- A duplicate copy of the signed Form 3115 should be sent to the IRS. The address varies depending on whether the change request is automatic or non-automatic (see 3115 instructions).

ONE LAST TAX PLANNING IDEA…
§45L ENERGY EFFICIENT HOME CREDIT

THE §45L ENERGY EFFICIENT HOME CREDIT

- A $2,000/unit Federal tax credit that promotes construction of energy efficient homes as well as encourages landlords to make improvements to existing residential units (3 stories or less).
- Requires independent certification to show to have an annual level of heating and cooling energy consumption of a “comparable dwelling unit” and has building envelope component improvements that account for at least 1/5 of the 50% reduction in energy consumption.
- This incentive was extended to include residences leased or sold through 2020 but will likely be extended.

THE §45L ENERGY EFFICIENT HOME CREDIT

- The residence or building must not be more than three stories above grade in height (high-rise residential may qualify under §179D).
- Examples of housing for which this credit applies includes:
  - Single Family Homes,
  - Townhouses,
  - Apartments,
  - Condominiums,
  - Assisted Living Homes, and
  - Student Housing.

THE §45L ENERGY EFFICIENT HOME CREDIT

- Taxpayer constructed a 250-unit apartment community with energy efficient features and at $2,000/unit, earned a $500,000 tax credit. The tax credit more than offset the costs for upgrades.

CONTACTS…

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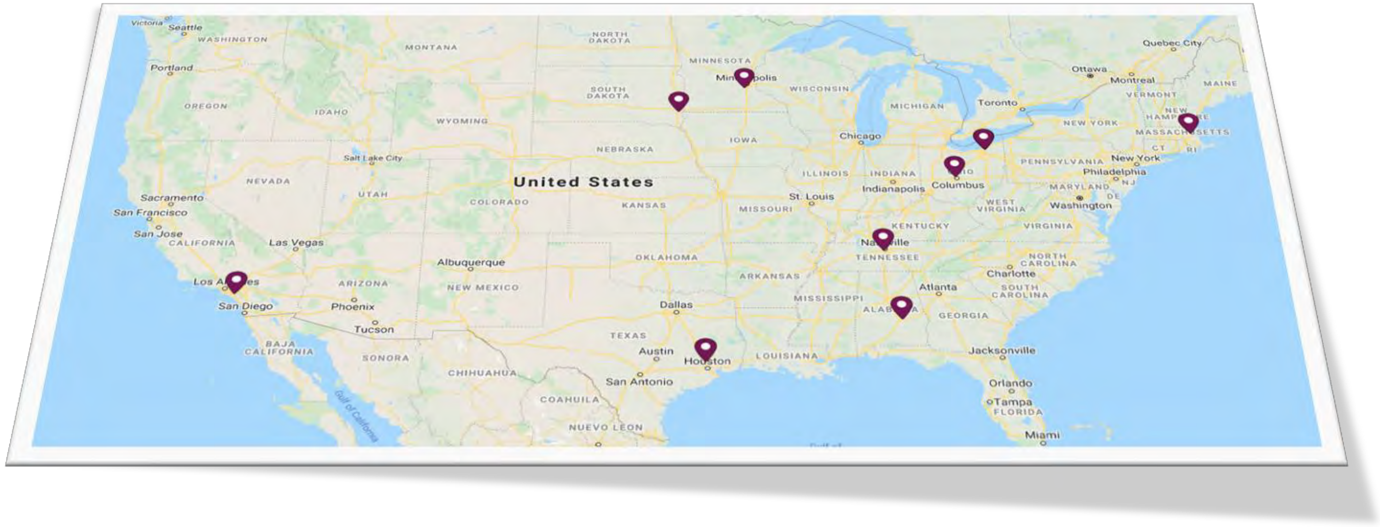

Locations:

Twin Cities Headquarters 8722 Egan Drive Savage MN 55378 877-427-8291	Northeast Ohio Office 3401 Enterprise Parkway 340 Beachwood OH 44122 216-870-0742	Central Ohio Office 3380 Tremont Road 220 Columbus OH 43221 614-456-7323
Northeast Office 70 Edgewood Street 1 Boston MA 02119 310-968-0970	Dakotas Office 7001 South Lyncrest Place 105 Sioux Falls SD 57108 605-929-6942	Southwest Office 2630 Hendricks Lakes Drive Spring TX 77388 512-215-1193
Pacific Coast Office 455 Estancia Irvine CA 92602 951-233-1562	Southeast Office 6831 Halcyon Park Drive Montgomery AL 36117 334-788-5721	South Central Office 6009 Sherwood Drive Nashville TN 37215 615-479-0881