



## ACCOUNTING PROCEDURES STATEMENT (EXPENSE VS. CAPITALIZATION)

The IRS has issued final regulations on the tax treatment of amounts paid to acquire, produce, or improve tangible property. The regulations explain when those payments can be deducted for an immediate tax benefit, and when they must be capitalized and subsequently depreciated. The regulations must be followed for 2022 tax returns.

**Capitalization or deduction:** The regulations set forth the general rule that amounts paid to improve a unit of property (UOP) must be capitalized. An improvement is defined as an expenditure that better a unit of property, restores it, or adapts it to a new and different use. On the other hand, the regulations allow a current deduction for repairs and maintenance to property only if not otherwise required to be capitalized.

**Materials and supplies:** A deduction is allowed for amounts paid to produce and acquire materials and supplies that are consumed during the year. Materials and supplies are defined to include five specific categories of property used or consumed in the business operations. For example, UOPs with an economic useful life of no more than 12 months qualify as materials and supplies under this rule. Likewise, UOPs that cost \$200 or less to acquire or produce, qualify as materials and supplies.

**De minimis safe harbor:** The regulations allow a taxpayer to deduct certain limited amounts paid for tangible property that are expensed for financial accounting purposes. For most businesses, the maximum figure is \$2,500 (previously \$500). The de minimis safe harbor amount paid for the property is per invoice, or per item as substantiated by the invoice. To use the safe harbor, a business must have accounting procedures in place at the beginning of the tax year that treat amounts paid for property costing less than a specified dollar amount or with an economic useful life of no more than twelve months as an expense.

**Routine maintenance safe harbor:** The regulations include a safe harbor that allows certain expenses of routine maintenance to be deducted rather than capitalized. Routine maintenance means recurring activities that keep business property (including buildings) in ordinarily efficient operating condition, such as inspections, cleaning, testing and replacement of damaged or worn parts. For a building structure or system, the taxpayer must reasonably expect to perform the maintenance more than once during the ten year period that begins when the structure or system is placed in service. For property other than buildings, the taxpayer must reasonably expect to perform the activities more than once during the depreciable life of the property.

### SAMPLE ANNUAL ACCOUNTING CAPITALIZATION POLICY

*(A new form must be signed each year.)*

Annual Accounting Capitalization Policy for \_\_\_\_\_  
*(taxpayer or business name)*

- (1) This accounting capitalization policy is effective as of 1/1/22, and treats as an expense for non-tax purposes:
  - (a) The amount paid for property that does not exceed \$2,500 per invoice (or per item as substantiated by the invoice); or
  - (b) The amount paid for property with an economic useful life of 12 months or less.
- (2) Pursuant to this policy, the amounts described in (1) above will be treated as an expense on the books and records.

\_\_\_\_\_  
Taxpayer signature

\_\_\_\_\_  
Date