

IRS Introduces Three New Automatic Method Changes and Provides Modified Procedures

Summary

On April 19, 2017, the Internal Revenue Service issued Revenue Procedure 2017-30 to update the list of automatic changes in methods of accounting to which the automatic change procedures under Rev. Proc. 2015-13 applies. In addition to adding three new automatic accounting method changes, the Rev. Proc. modifies existing automatic method changes, removes certain obsolete method changes, and provides limited transition rules.

For federal income tax purposes, once a taxpayer has adopted or established a method of accounting, that method, whether proper or improper, must continue to be used until the taxpayer files a Form 3115, *Application for Change in Accounting Method*, to secure the Service's consent to change to a different method. Taxpayers should carefully review the more than two hundred automatic method changes listed in Rev. Proc. 2017-30 to identify any opportunities to file automatic method change request to secure the Service's consent to change to the proper or most optimal method of accounting in order to address any exposures, reduce taxable income and increase cash tax savings.

Rev. Proc. 2017-30 generally supersedes Rev. Proc. 2016-29 and is effective for automatic accounting method change requests filed on or after April 19, 2017, for a taxable year of change ending on or after August 31, 2016. In light of the immediate effective date of this revenue procedure, all Form 3115 requests filed under the automatic procedures set forth in Rev. Proc. 2015-13 must now be filed pursuant to this new procedure.

New Automatic Method Changes

Rev. Proc. 2017-30 contains a list of over two hundred automatic method changes. In general, if the method change is identified as automatic by the Service, the Form 3115 request is subject to lower IRS scrutiny (i.e., the taxpayer is deemed to have "automatic consent" to change to the new method of accounting), no user fee, and an extended deadline for filing the request. If a method change is not identified as automatic by the Service or the taxpayer did not meet an eligibility requirement under Rev. Proc. 2015-13, the taxpayer is required to file a non-automatic Form 3115. A non-automatic change is subject to greater IRS scrutiny, requires an IRS user fee, and must be filed no later than the last day of the year of change. A favorable development in Rev. Proc. 2017-30 is the addition of the following three new automatic method change procedures:

- **Organizational expenditures under Section 248 (Automatic Change #228):** This new automatic procedure applies to a change in the characterization of an item as an organizational expenditure; the determination of the taxable year in which the corporation begins business to which the organizational expenditures relate; or the amortization of an organization expenditure to 180 months.

- **Organization fees under Section 709 (Automatic Change #229):** This new automatic procedure applies to a partnership that wants to change the characterization of an item as an organization expense; the determination of the taxable year in which the partnership begins business to which the organizational expenses relate; or the amortization period of an organizational expense to 180 months.
- **Change from currently deducting inventories to permissible methods of identification and valuation of inventories (Automatic Change #230):** This new automatic procedure applies to a taxpayer changing from currently deducting inventories to a permissible method of identifying and valuing inventories. For example, a taxpayer currently deducting inventories may change to using the first-in, first-out (FIFO) method as its inventory-identification method and cost or market, whichever is lower (LCM), as its inventory-valuation method.

Modifications to Existing Method Changes

Rev. Proc. 2017-30 sets forth certain significant changes, among others, to existing automatic method changes. Several of the method changes that were previously automatic, including the change to make a late partial disposition election and the revocation of a taxpayer's general asset account election, were removed in their entirety from the list, as they are now obsolete. Additionally, the Service removed temporary waivers of certain eligibility rules applicable to specific method changes for which the waivers expired in previous years.

Aside from the removal of several method changes and eligibility rule waivers, Rev. Proc. 2017-30 also revises certain terms and conditions of numerous automatic method changes remaining on the list. Some of the key modifications set forth under Rev. Proc. 2017-30 include the following:

- **Start-up expenditures (Automatic Change #223):** The new revenue procedure now includes a change in the amortization period of a start-up expenditure to 180 months.
- **Deducting repair and maintenance costs (Automatic Change #184):** The new revenue procedure specifies that the automatic change procedures do not apply to amounts paid or incurred for repair and maintenance costs that the taxpayer is changing from capitalizing to deducting and for which the taxpayer has received a payment for specified energy property in lieu of tax credits under Section 1603.
- **Section 467 rent (Automatic Change #136):** Previously, rental agreements providing a specific allocation of fixed rent as described in Reg. Section 1.467-1(c)(2)(ii)(A)(2) were excluded from the automatic change procedures. The new revenue procedure modifies the language to clarify that the automatic provisions do not apply to rental agreements that provide a specific allocation of fixed rent that allocate rent to periods other than when such rents are payable.

- **Mark-to-market accounting (Automatic Change #64):** Rev. Proc. 2017-30 modifies the existing automatic method change to provide that the eligibility rule in Section 5.01(1)(d) of Rev. Proc. 2015-13 (generally precluding a taxpayer from filing an automatic method change in the final year of its trade or business) does not apply to this change.

There are numerous modifications in Rev. Proc. 2017-30 that are not addressed above. Therefore, it is prudent to review the relevant section(s) of the revenue procedure pertaining to the method change(s) at issue to ensure that the taxpayer is able to make the method change under the automatic change procedures.

Effective Date and Limited Transition Relief

Rev. Proc. 2017-30 is effective for automatic accounting method change requests filed on or after April 19, 2017, for a taxable year of change ending on or after August 31, 2016.

Rev. Proc. 2017-30 provides transition rules for Form 3115 requests that were previously filed under the non-automatic method change procedures where the applicable method change is now an automatic method change. If the non-automatic Form 3115 was filed prior to April 19, 2017, under Rev. Proc. 2015-13 and remains pending with the IRS National Office as of that date, the taxpayer may notify the Service to convert the application into an automatic change.

In addition, Rev. Proc. 2017-30 eliminated certain automatic method changes previously available under the now-superseded Rev. Proc. 2016-29. By default, such method changes must now be filed under the non-automatic change procedures of Rev. Proc. 2015-13. If the taxpayer properly filed the original or the duplicate copy of a Form 3115 under the prior automatic change procedures before April 19, 2017, that method change remains automatic. However, if the taxpayer did not properly file the original or the duplicate copy of such Form 3115, that method change must be filed non-automatically.

Insights

Rev. Proc. 2017-30 reflects the Service's continued efforts to expand the list of automatic changes available to taxpayers. As these changes generally are easier to implement in comparison to those filed under the non-automatic change procedures, the recent additions to the list of automatic changes represents a welcome relief from many of the administration burdens associated with making a change in method of accounting. Further, the Service has indicated informally that it intends to revisit the list of automatic changes on a regular basis, and is open to feedback from taxpayers and practitioners as to whether any method changes that are presently non-automatic - particularly those that are fairly straightforward and uncontroversial from a tax accounting perspective - should be added to the list of automatic changes.