

REPAIR & MAINTENANCE REGULATIONS

FLOW CHART: SHOULD I CAPITALIZE OR EXPENSE

Step 1:

Materials and Supplies	
Will the item (that is not inventory but is used to maintain, repair, or improve property: i.e. fuel, lubricants, water, etc.) be consumed in the ordinary course of business within 1 year or does the item have an economic useful life of less than 12 months?	
YES	NO
Does the item cost less than \$200?	Go to Step 2
YES	NO
Expense	Go to Step 2

Step 2:

De Minimis Safe Harbor	
Do you have a written capitalization policy in place at the BEGINNING of the tax year?	
YES	NO
Is the safe harbor amount lower than the IRS thresholds:	Go to Step 3
→ \$5,000 per item with applicable financial statements	
→ \$500 per item without applicable financial statements	
YES	NO
The capitalization policy should be adjusted to conform with IRS regulations	
Does the item you're looking at fall below the de minimis threshold stated in the capitalization policy?	
YES	NO
Expense	Go to Step 3

Step 3:

Routine Maintenance Safe Harbor	
Is this the first time incurring this expenditure?	
YES	NO
Expenditure should be capitalized	
Can you reasonably expect to perform this activity more than once during the useful life of the asset?	
→ Buildings have a 10-year useful life for this rule	
→ Use the ADS useful life for all other assets	
YES	NO
Expense	Go to Step 4

Step 4:

Small Taxpayer Safe Harbor	
Is the item in question eligible building property?	
YES	NO
Are your average annual gross receipts for the preceding 3 years ≤ \$10 Million?	Go to Step 5
YES	NO
Is the unadjusted basis of the building ≤ \$1 Million?	Go to Step 5
YES	NO
Does the total amount paid throughout the year for repairs, maintenance, improvements, etc. on the eligible building property exceed the lesser of 1) 2% of the building's unadjusted basis or 2) \$10,000?	Go to Step 5
YES	NO
Go to Step 5	Expense

Step 5:

Capitalization Standards	
You should now consider the unit of property and RABI (restoration, adaptation, betterment, and improvement) rules to determine if the item should be capitalized or expensed. These rules are more complex and might require an in-depth analysis; feel free to contact your BNN tax advisor.	
Identify Property to be Tested	
<u>Non-Buildings</u> * Plant Property * Network Assets * All Other	<u>Buildings</u> * Structure * Systems
Betterments	
Does the expenditure correct a pre-existing defect?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Does the expenditure materially add to or expand the property?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Does the expenditure materially increase quality, capacity, productivity, or efficiency?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Adaptation	
Has the property been adapted to a new or different use?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Restoration	
Does the expenditure replace a component for which the Taxpayer recognized a gain/loss on sale or disposition?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Does the expenditure restore damage resulting from a casualty event?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Does the expenditure return the property to an operable condition after falling into a state of disrepair?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Does the expenditure replace a major component or substantial structural part?	
YES	NO
CAPITALIZE Go to Step 6	Go to next test
Does the expenditure rebuild the property to a "like new" condition after the end of its class life?	
YES	NO
CAPITALIZE Go to Step 6	EXPENSE Cost qualifies as Repairs and Maintenance Expense
Step 6: Expenditure is capitalized - Consider PAD	
You should now consider disposing of the old asset. Taxpayer is entitled to make a disposal of the asset replaced by the current addition.	