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26 CFR 601.204: Changes in accounting periods and in methods of accounting. (Also Part 1, §§ 167, 168, 197, 446; 1.167(e)-1, 1.446-1)

## Rev. Proc. 96-31

### SECTION 1. PURPOSE

This revenue procedure provides an automatic consent procedure that permits a taxpayer who has claimed less than the depreciation or amortization allowable to change the taxpayer's method of accounting to claim allowable depreciation or amortization. The omitted depreciation or amortization from years prior to the year of change will be taken into account through a § 481(a) adjustment. The taxpayer has the option of either making the method change under this revenue procedure or requesting permission to make the method change under Rev. Proc. 92-20, 1992-1 C.B. 685 (or any successor).

### SECTION 2. BACKGROUND

.01 A change from not claiming the depreciation or amortization allowable (hereafter, depreciation means depreciation or amortization) to claiming the depreciation allowable is a change in method of accounting for which the consent of the Commissioner of Internal Revenue is required. Sections

1.167(e)-1(a) and 1.446-1(e)(2)(ii)(b) of the Income Tax Regulations.

.02 To obtain this consent, a Form 3115, Application for Change in Accounting Method, generally must be filed within 180 days after the beginning of the taxable year in which the proposed change is to be made. Section 1.446-1(e)(3)(i).

.03 The Commissioner is authorized to prescribe administrative procedures setting forth the limitations, terms, and conditions as the Commissioner deems necessary to obtain consent for effecting a change in method of accounting and to prevent amounts from being duplicated or omitted, including the taxable year or years in which the § 481(a) adjustment is to be taken into account. Section 1.446-1(e)(3)(ii).

.04 In computing taxable income, § 481(a) of the Internal Revenue Code requires a taxpayer to take into account those adjustments necessary to prevent amounts from being duplicated or omitted when the taxpayer's taxable income is computed under a method of accounting different from the method used to compute taxable income for the preceding taxable year.

.05 The basis of depreciable property is reduced by the amount of the depreciation allowed or allowable, whichever is greater. Section 1016(a)(2).

.06 Unless otherwise provided in this revenue procedure, the terms "taxpayer", "year of change", and "filed" have the meaning given to them by sections 3.01, 3.03, and 3.04 of Rev. Proc. 92-20 (or any successor), respectively.

### SECTION 3. SCOPE

.01 *Application of this revenue procedure.* Except as provided in sections 3.02 and 3.03 of this revenue procedure, this revenue procedure applies to any taxpayer changing to a permissible method of accounting for depreciation for any item of property that: (1) under the taxpayer's present method of accounting, the taxpayer has not taken into account any depreciation allowance or has taken into account some depreciation but less than the depreciation allowable (hereafter, referred to as claimed less than the depreciation allowable); (2) is subject to § 167,

§ 168, § 197, or § 168 prior to its amendment in 1986 (former § 168); and (3) is held by the taxpayer as of the beginning of the year of change.

.02 *Non-application of this revenue procedure.* This revenue procedure does not apply to:

(1) Any property to which § 1016(a)(3) (generally relating to property held by a tax-exempt organization) applies;

(2) Any intangible property subject to § 167, except for property subject to § 167(f) (pertaining to certain property excluded from § 197);

(3) Any property for which a taxpayer is seeking either to revoke a timely election, or to make a late election, under § 167, § 168, former § 168, or § 13261(g)(2) or (3) of the Revenue Reconciliation Act of 1993 (the "1993 Act"), 1993-3 C.B. 1, 128 (relating to amortizable § 197 intangibles). A taxpayer may request consent to revoke or make the election by submitting a request for a letter ruling under Rev. Proc. 96-1, 1996-1 I.R.B. 8 (or any successor);

(4) Except for property subject to § 167(f), any property subject to § 167 for which a taxpayer is changing only the estimated useful life of the property. A change in the estimated useful life of property subject to § 167 must be made prospectively. *See, e.g.*, § 1.167(b)-2(c);

(5) Any depreciable property that changes use but continues to be owned by the same taxpayer. *See, e.g.*, § 168(i)(5);

(6) Any property for which a taxpayer has claimed depreciation in excess of the depreciation allowable;

(7) Any change in method of accounting involving a change from deducting the cost or other basis of any property as an expense to capitalizing and depreciating the cost or other basis;

(8) Any change in method of accounting involving a change from one permissible method of accounting for the property to another permissible method of accounting for the property. For example, a:

(a) Change from the straight-line method of depreciation to the income forecast method of depreciation for videocassettes. *See* Rev. Rul. 89-62, 1989-1 C.B. 78; or

(b) Change from charging the depreciation reserve with costs of removal and crediting the depreciation

reserve with salvage proceeds to deducting costs of removal as an expense and including salvage proceeds in taxable income. *See* Rev. Rul. 74-455, 1974-2 C.B. 63; or

(9) Any change in method of accounting for an item of income or deduction other than depreciation even if a taxpayer's present method of accounting may have resulted in the taxpayer claiming less than the depreciation allowable. For example, a change in accounting method involving a:

(a) Change in inventory costs (for example, when property is reclassified from inventory property to depreciable property); or

(b) Change in the character of a transaction from sale to lease.

.03 *Taxpayer under criminal investigation or proceeding.* If a criminal investigation or proceeding is pending concerning (1) any issue directly or indirectly related to a taxpayer's federal tax liability for any taxable year, or (2) the possibility of false or fraudulent statements made by the taxpayer regarding any issue related to the taxpayer's federal tax liability for any taxable year, this revenue procedure does not apply to the taxpayer.

.04 *Procedures available when a method change may not be made under this revenue procedure.* If a change in accounting method is not permitted under this revenue procedure solely by reason of section 3.02(1), 3.02(2), 3.02(6), 3.02(7), 3.02(8), or 3.02(9) of this revenue procedure, a taxpayer must file a Form 3115 in accordance with the requirements of either Rev. Proc. 92-20 (or any successor) or any other applicable revenue procedure pertaining to the method change. Thus, for example, if a taxpayer wants to change from claiming more than the depreciation allowable on some items of property but also opts to use this revenue procedure to change from claiming less than the depreciation allowable on other items of property, the taxpayer must file two Forms 3115—one Form 3115 under Rev. Proc. 92-20 (or any successor) for the over-depreciated property and one Form 3115 under this revenue procedure for the under-depreciated property. The taxpayer, however, files one Form 3115 if the taxpayer uses Rev. Proc. 92-20 (or any successor) to change the method of accounting for both the under- and over-depreciated properties.

## SECTION 4. CONSENT TO CHANGE

.01 *Consent granted.* The consent of the Commissioner under § 1.446-1(e)-(2)(i) is granted to any taxpayer within the scope of this revenue procedure to make a method change to a permissible method of accounting for depreciation for any item of property within the scope of this revenue procedure. This consent is granted, however, only if the taxpayer complies with section 5 of this revenue procedure. If the taxpayer does not comply with section 5 of this revenue procedure, the taxpayer will be deemed to have initiated a change in method of accounting without obtaining the consent of the Commissioner required under § 446(e).

.02 *Effect of consent.* The consent that is granted under this revenue procedure does not constitute an opinion of the Commissioner regarding the propriety of a taxpayer's proposed method of accounting. Consequently, if the proposed method of accounting is an impermissible method of accounting, the Service may change the taxpayer's proposed method of accounting to a permissible method of accounting in any open year.

## SECTION 5. MANNER OF EFFECTING AUTOMATIC CHANGE

.01 *General procedure.*

(1) *Complete and file a current Form 3115.* A taxpayer makes a change in method of accounting under this revenue procedure by completing and filing a current Form 3115 in duplicate. The original of the Form 3115 must be filed with the Office of Associate Chief Counsel (Domestic) (national office) on or before 180 days after the beginning of the year of change and addressed to the Commissioner of Internal Revenue, Attn: CC:DOM:P&SI:6, Room 5112, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. In addition, a copy of the Form 3115 must be attached to the taxpayer's timely filed (including extensions) federal income tax return for the year of change.

The 180-day filing period begins on the first day of any taxable year. If the taxable year is a short taxable year (less than 12 full months), the original of the Form 3115 must be filed with the national office no later than 180

days after the beginning of the short taxable year or, if earlier, no later than the last day of the short taxable year.

In completing the current Form 3115 (Rev. February 1996), the taxpayer must complete Schedule D, Part II, Change in Depreciation or Amortization (page 7 of the Form 3115), and any other applicable schedule. With respect to Parts I through III on pages 1 and 2 of the current Form 3115, the taxpayer must provide only the information requested on the following lines:

(a) Part I, Eligibility To Request Change (page 1)-lines 1, 2a and b, and 6;

(b) Part II, Description of Change (page 2)-line 8 and to the extent not provided elsewhere on the Form 3115, lines 10, 11, 12, 13, 17, 18a and b, and 19; and

(c) Part III, Section 481(a) Adjustment (page 2)-lines 20, 22, 23, and 25.

(2) *Label.* The taxpayer should type or legibly print at the top of the Form 3115: "AUTOMATIC METHOD CHANGE UNDER REV. PROC. 96-31."

(3) *No user fee and acknowledgment.* No user fee is required for a Form 3115 filed under this revenue procedure and a Form 3115 filed pursuant to this revenue procedure will not be acknowledged.

.02 *Permissible method of accounting for depreciation must be used.* A taxpayer must change to a permissible method of accounting for depreciation for the item of property. This method is the same method that determines the depreciation allowable for the item of property (as determined under section 7 of this revenue procedure).

.03 *Year of change.* The year of change is the taxable year for which the original of the Form 3115 is considered timely filed with the national office under section 5.01(1) of this revenue procedure.

.04 *Section 481(a) adjustment.*

(1) *In general.* A change in method of accounting under this revenue procedure is treated as a voluntary change in method of accounting that is initiated by the taxpayer and, therefore, the § 481(a) adjustment is not restricted to post-1953 items.

(2) *Amount of § 481(a) adjustment.* The § 481(a) adjustment is a negative § 481(a) adjustment (decrease in taxable income) to prevent the

omission of the allowable but unclaimed depreciation for open and closed years prior to the year of change. This negative § 481(a) adjustment equals the difference between the total amount of depreciation taken into account in computing taxable income for the property under the taxpayer's present method of accounting, and the total amount of depreciation allowable for the property under the taxpayer's proposed method of accounting (as determined under section 7 of this revenue procedure), for any taxable year prior to the year of change. The amount of the negative § 481(a) adjustment, however, must be offset by any allowable but unclaimed depreciation that is required to be capitalized under any provision of the Code (for example, § 263A) as of the beginning of the year of change.

(3) *Section 481(a) adjustment period.* A taxpayer must take the entire negative § 481(a) adjustment into account in computing the taxable income in the year of change.

.05 *Basis adjustment.* The basis of depreciable property to which this revenue procedure applies must reflect the reductions required by § 1016(a)(2) for the depreciation allowable for the property (as determined under section 7 of this revenue procedure).

## SECTION 6. REVIEW OF FORM 3115

The Form 3115 will be subject to review by the national office. In addition, the facts underlying the method change, including the amount of any § 481(a) adjustment and any § 1016(a)(2) adjustment to the basis of the property, will be subject to verification by the district director. If the Form 3115 is reviewed and the taxpayer's proposed method of accounting appears to be an impermissible method of accounting for depreciation or the taxpayer or property appears to be outside the scope of this revenue procedure, the national office or the district director will notify the taxpayer, in writing, that consent is not granted under this revenue procedure. The taxpayer then may complete and file a new Form 3115 under this revenue procedure or Rev. Proc. 92-20 (or any successor), as applicable. The year of change for this new Form 3115 will be determined in accordance with the requirements of such revenue procedure.

## SECTION 7. MEANING OF DEPRECIATION ALLOWABLE

.01 *In general.* This section 7 discusses the amount of the depreciation allowable determined under § 167, § 168, § 197, or former § 168. This amount, however, may be limited under other provisions of the Code (for example, § 280F).

.02 *Section 167 property.* Generally, for any taxable year, the depreciation allowable for property subject to § 167 is determined either: (1) under the depreciation method adopted by a taxpayer for the property; or (2) if this depreciation method does not result in a reasonable allowance for depreciation or a taxpayer has not adopted a depreciation method for the property, under the straight-line depreciation method. For determining the estimated useful life and salvage value of the property, see § 1.167(a)-1(b) and (c), respectively. The depreciation allowable for any taxable year for property subject to § 167(f) (pertaining to certain property excluded from § 197) is determined by using the depreciation method and useful life prescribed in § 167(f).

.03 *Section 168 property.* The depreciation allowable for any taxable year for property subject to § 168 is determined by using either: (1) the general depreciation system in § 168(a); or (2) the alternative depreciation system in § 168(g) if the property is required to be depreciated under the alternative depreciation system pursuant to § 168(g)(1) or other provisions of the Code (for example, property described in § 263A(e)(2)(A) or § 280F(b)(1)). Property required to be depreciated under the alternative depreciation system pursuant to § 168(g)(1) includes property in a class for which the taxpayer made a timely election under § 168(g)(7).

.04 *Section 197 property.* The depreciation allowable for any taxable year for an amortizable § 197 intangible (including any property for which a timely election under § 13261(g)(2) of the 1993 Act was made) is determined by using the straight-line method over a 15-year period.

.05 *Former § 168 property.* The depreciation allowable for any taxable year for property subject to former § 168 is determined by using either: (1) the accelerated method of cost recovery applicable to the property (for example,

for 5-year property, the recovery method under former § 168(b)(1)); or (2) the straight-line method applicable to the property if the property is required to be depreciated under the straight-line method (for example, property described in former § 168(f)-(12) or former § 280F(b)(2)) or if the taxpayer elected to determine the depreciation allowance under the optional straight-line percentage (for example, the straight-line method in former § 168(b)(3)).

## SECTION 8. EFFECTIVE DATE

.01 *In general.* This revenue procedure is effective May 13, 1996.

.02 *Form 3115 already pending with the Service.*

(1) *In general.* The provisions of this revenue procedure apply to a taxpayer with a Form 3115 (including a Form 3115 filed under the early application provision of section 5.01(3) of Rev. Proc. 92-20) timely filed with the Service as of May 13, 1996, for a method change for depreciation to which this revenue procedure applies. Therefore, the taxpayer has the option to make the method change under this revenue procedure or to request permission to make the method change under Rev. Proc. 92-20 (or any successor). In this regard, the taxpayer must notify the national office, in writing, on or before August 15, 1996, as to the taxpayer's decision. If the national office is not notified by August 15, 1996, the Form 3115 will be treated as filed under Rev. Proc. 92-20.

(2) *Manner of effecting automatic change.* If the taxpayer makes the method change under this revenue procedure, the taxpayer's Form 3115 timely filed as of May 13, 1996, will be treated as being timely filed with the national office under this revenue procedure. The original of the Form 3115 will be retained by the national office. The national office will return a copy of the Form 3115 to the taxpayer so that, as required, the taxpayer can attach the copy to the taxpayer's timely filed (including extensions) original federal income tax return, or to an amended return, for the year of change. The receipt of this copy is not an opinion of the Commissioner regarding the propriety of the taxpayer's proposed method of accounting. See section 4.02 of this revenue procedure.

If all of the property subject to the Form 3115 appears to be within the

scope of this revenue procedure and the taxpayer notifies the national office in a timely manner that the taxpayer is making the method change under this revenue procedure, any user fee submitted with the Form 3115 will be returned to the taxpayer.

(3) *Year of change.* For a taxpayer with a Form 3115 timely filed as of May 13, 1996, the taxpayer may make the method change under this revenue procedure either for the year of change originally requested on the Form 3115 (or if this year is a closed year, for the first subsequent open year) or for the taxpayer's taxable year beginning in 1995 or 1996. If the taxpayer modifies the year of change, the taxpayer must submit a letter to the national office, stating the new year of change and any revised information on the taxpayer's Form 3115 to reflect the new year of change (for example, the revised § 481(a) adjustment for the year of change). This letter must be submitted on or before August 15, 1996, to the national office. If the national office is not notified by August 15, 1996, the year of change is the one originally requested on the taxpayer's Form 3115 (or if this year is a closed year, the first subsequent open year).

If the taxpayer makes the method change under this revenue procedure for under-depreciated property but the Form 3115 also includes items of property for which the taxpayer, under the taxpayer's present method of accounting, claimed more than the depreciation allowable, the year of change for the over-depreciated property will be the same as the year of change for the under-depreciated property.

(4) *Submission of additional information.* The additional information requested in section 8.02(1) and (3) of this revenue procedure must be accompanied by the following penalties of perjury statement: "Under penalties of perjury, I declare that I have examined this request, including accompanying documents, and to the best of my knowledge and belief, the facts presented in support of the requested Form 3115 are true, correct, and complete." This penalties of perjury statement must be signed and dated by the taxpayer, not the taxpayer's representative. Also, a stamped signature is not permitted.

The additional information (including the penalties of perjury statement) must

be addressed to the Commissioner of Internal Revenue, Attn: CC:DOM: P&SI:6, Room 5112, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

## SECTION 9. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 92-20 is modified.

## DRAFTING INFORMATION

The principal author of this revenue procedure is Kathleen Reed of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). For further information regarding this revenue procedure, contact Ms. Reed at (202) 622-3110 (not a toll-free number).