Section 59.—Other Definitions and Special Rules

26 CFR 1.59–1: Optional 10-year writeoff of certain tax preferences.

T.D. 9168

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Parts 1 and 602

Optional 10-Year Writeoff of Certain Tax Preferences

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulation.

SUMMARY: This document contains final regulations relating to the optional 10-year writeoff of certain tax preference items under section 59(e) of the Internal Revenue Code (Code). The final regulations affect taxpayers who utilize section 59(e) for the optional 10-year writeoff of certain tax preferences. These final regulations provide guidance on the time and manner of making an election under section 59(e). The regulations also provide guidance on revoking an election under section 59(e). The regulations reflect changes to the law made by the Tax Reform Act of 1986, the Technical and Miscellaneous Revenue Act of 1988, and the Omnibus Budget Reconciliation Act of 1989.

DATES: *Effective Date:* These regulations are effective December 22, 2004.

Applicability Date: These regulations apply to a section 59(e) election made for a taxable year ending, or a request to revoke a section 59(e) election submitted, on or after December 22, 2004.

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in these final regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)) under control number 1545–1903. Responses to this collection of information are required to obtain the benefit of the section 59(e) election.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number assigned by the Office of Management and Budget.

The estimated annual burden per respondent is one hour.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224, and to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document contains amendments to 26 CFR part 1 under section 59(e) of the Code. Section 59(e)(1) allows taxpayers to elect to deduct any qualified expenditure ratably over a 10-year period (3-year period in the case of circulation expenditures described in section 173) beginning with the taxable year in which the expenditure was made (or, in the case of a qualified expenditure under section 263(c), over the 60-month period beginning with the month in which such expenditure was paid or incurred). Section 59(e)(2) defines *qualified expenditure* as any amount that, but for an election under section 59(e), would have been allowed as a deduction (determined without regard to section 291) for the taxable year in which paid or incurred under section 173 (relating to circulation expenditures), section 174 (relating to research and experimental expenditures), section 263(c) (relating to intangible drilling and development expenditures), section 616(a) (relating to development expenditures), or section 617(a) (relating to mining exploration expenditures).

Section 59(e)(4)(A) states that an election under section 59(e) (section 59(e) election) may be made with respect to any portion of any qualified expenditure. The legislative history of section 59(e) suggests that this allows a section 59(e) election to be made "dollar for dollar." *See* H.R. Rep. 99–426, 99th Cong., 1st Sess. 327 (1985), 1986–3 (Vol. 2) C.B. 1, 327; S. Rep. No. 99–313, 99th Cong., 2d Sess. 539 (1986), 1986–3 (Vol. 3) C.B. 1, 539.

Section 59(e)(4)(B) states that a section 59(e) election may only be revoked with the consent of the Secretary.

Provisions similar to those currently contained in section 59(e) were originally enacted as section 58(i) under the Tax Equity and Fiscal Responsibility Act of 1982 (Public Law 97–248; 96 Stat. 324). Under section 58(i)(1), the optional 10-year writeoff was available only to individuals. Section 58(i)(5)(C) directed the Secretary to promulgate regulations governing the time and manner for making an election under section 58(i) (section 58(i) election).

Section 5f.0(a)(2)(i)(A) and (B) of the temporary Income Tax Regulations that were promulgated under section 58(i) required that a section 58(i) election be made by the later of the due date (including extensions) of the income tax return for the taxable year for which the election was to be effective, or April 15, 1983. T.D. 7870, 1983–1 C.B. 13 [48 FR 1486]. Section 5f.0(a)(3) provided that a section 58(i) election was made by attaching a statement to the income tax return (or amended return) for the taxable year in which the election was made. Section 5f.0 was redesignated as §301.9100–5T by T.D. 8435, 1992–2 C.B. 324 [57 FR 43893], on October 15, 1992.

Section 59(e) was enacted as part of the Tax Reform Act of 1986 (Public Law 99–514; 100 Stat. 2085) and, unlike section 58(i), is not limited to individuals. While both the Senate Finance Committee

Report and the House Ways and Means Committee Report state that the time and manner of the election would be governed by regulations, Congress did not include a provision similar to former section 58(i)(5)(C) directing the Secretary to promulgate regulations governing the time and manner for making a section 59(e) election. *See* H.R. Rep. No. 99–426, 99th Cong., 1st Sess. 327 (1985), 1986–3 (Vol. 2) C.B. 1, 327; S. Rep. No. 99–313, 99th Cong., 2d Sess. 539 (1986), 1986–3 (Vol. 3) C.B. 1, 539.

A notice of proposed rulemaking (REG–124405–03, 2004–35 I.R.B. 394 [69 FR 43367]) was published in the **Federal Register** on July 20, 2004. Two requests for a public hearing were received. A public hearing was held on December 7, 2004. The IRS received written and electronic comments responding to the notice of proposed rulemaking. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury decision. The revisions are discussed below.

Summary of Comments and Explanation of Revisions

Several commentators recommended changes regarding the information taxpayers would be required to submit as part of their section 59(e) election. Specifically, commentators requested that the IRS reconsider §1.59–1(b)(1)(ii) and (iii) of the proposed regulations, which would require taxpayers to identify (i) the type and amount, for each activity or project, of qualified expenditures identified in section 59(e)(2) the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1), and (ii) a description of each specific activity or project to which the qualified expenditures relate. The commentators suggest that the majority of taxpayers who incur research and experimentation expenditures under section 174(a) and make a section 59(e) election with respect to such expenditures do not currently maintain records on a project-by-project basis. As a result, the commentators stated that requiring taxpayers to account for their section 59(e) qualified expenditures on a project-by-project basis would be a financial and administrative burden. Some of the commentators also discussed section 1016(a)(20), which provides that proper adjustment in respect of the property shall in all cases be made for amounts allowed as deductions under section 59(e) (relating to optional 10-year writeoff of certain tax preferences). Compliance with section 1016(a)(20) requires that taxpayers be able to account for their section 59(e) expenditures through appropriate basis adjustments for each property, project, or activity.

Sections 1.59–1(b)(1)(ii) and (iii) of the proposed regulations were intended to improve compliance with section 1016(a)(20) by requiring that section 59(e) qualified expenditures be allocated among the properties, projects or activities to which they relate. Comments received regarding this provision indicate that, for taxpayers incurring section 174(a) expenditures, the basis rules of section 1016(a)(20) are only of importance when a project to which a section 59(e) election relates is disposed of, and that it is rare for a research project to be disposed of prior to the full amortization of the allocable section 59(e) qualified expenditures. As such, the commentators argue that the burden of requiring taxpayers to identify on a section 59(e) election the type and amount of qualified expenditures for each activity or project greatly exceeds the potential harm caused by non-compliance with section 1016(a)(20).

Having fully considered all comments received, the final regulations are modified to reflect the comments discussed above. Taxpayers making a section 59(e) election will not be required to identify on the election the type and amount of qualified expenditures for each activity or project nor will they be required to provide a description of each specific activity or project to which the qualified expenditures relate. Instead, taxpayers will be required only to identify the type and amount of qualified expenditures identified in section 59(e)(2) that the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1). However, taxpayers remain responsible for full compliance with the requirements of section 1016(a)(20). Specifically, taxpayers who allocate their section 59(e) expenditures to reduce the gain otherwise recognized on the disposition of a property, project, or activity must maintain books and records sufficient to support that allocation.

The preamble to the proposed regulations stated that, with respect to an otherwise valid section 59(e) election filed for a taxable year ending prior to the effective date of the final regulations, such election would not be challenged by the IRS merely because the election was made later than the date prescribed by law for filing the taxpayer's original income tax return (including any extensions of time) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. One commentator requested guidance on what the IRS considers an otherwise valid section 59(e) election filed for a tax year ending prior to the effective date of the final regulations. Although the IRS will treat a section 59(e) election prepared in a manner described in the final regulations as sufficient for a tax year ending prior to the effective date of the final regulations, because the final regulations only apply prospectively the final regulations do not provide guidance on what constitutes an otherwise valid section 59(e) election filed for a tax year prior to the effective date of the final regulations.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that the collection of information in these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that the reporting burden, as discussed earlier in this preamble, is expected to be insignificant. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding this regulation was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these final regulations is Eric B. Lee of the Office of As-

sociate Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

Paragraph 1. The authority citation for part 1 reads, in part, as follows:

Authority: 26 U.S.C. 7805, * * *

Par. 2. Section 1.59–1 is added to read as follows:

§1.59–1 Optional 10-year writeoff of certain tax preferences.

(a) *In general*. Section 59(e) allows any qualified expenditure to which an election under section 59(e) applies to be deducted ratably over the 10-year period (3-year period in the case of circulation expenditures described in section 173) beginning with the taxable year in which the expenditure was made (or, in the case of intangible drilling and development costs deductible under section 263(c), over the 60-month period beginning with the month in which the expenditure was paid or incurred).

(b) *Election*—(1) *Time and manner of election*. An election under section 59(e) shall only be made by attaching a statement to the taxpayer's income tax return (or amended return) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. The statement must be filed no later than the date prescribed by law for filing the taxpayer's original income tax return (including any extensions of time) for the taxable year in which the amortization of the qualified expenditures subject to the section 59(e) election begins. Additionally, the statement must include the following information —

(i) The taxpayer's name, address, and taxpayer identification number; and

(ii) The type and amount of qualified expenditures identified in section 59(e)(2) that the taxpayer elects to deduct ratably over the applicable period described in section 59(e)(1).

(2) *Elected amount*. A taxpayer may make an election under section 59(e) with respect to any portion of any qualified expenditure paid or incurred by the taxpayer in the taxable year to which the election applies. An election under section 59(e) must be for a specific dollar amount and the amount subject to an election under section 59(e) may not be made by reference to a formula. The amount elected under section 59(e) is properly chargeable to a capital account under section 1016(a)(20), relating to adjustments to basis of property.

(c) *Revocation*—(1) *In general*. An election under section 59(e) may be revoked only with the consent of the Commissioner. Such consent will only be granted in rare and unusual circumstances. The revocation, if granted, will be effective in the first taxable year in which the section 59(e) election was applicable. However, if the period of limitations for the first taxable year the section 59(e) election was applicable has expired, the revocation, if granted, will be effective in the earliest taxable year for which the period of limitations has not expired.

(2) *Time and manner for requesting consent*. A taxpayer requesting the Commissioner's consent to revoke a section 59(e) election must submit the request prior to the end of the taxable year the applicable amortization period described in section 59(e)(1) ends. The application for consent to revoke the election must be submitted to the Internal Revenue Service in the form of a letter ruling request.

(3) *Information to be provided*. A request to revoke a section 59(e) election must contain all of the information necessary to demonstrate the rare and unusual circumstances that would justify granting revocation.

(4) *Treatment of unamortized costs*. The unamortized balance of the qualified expenditures subject to the revoked section 59(e) election as of the first day of the taxable year the revocation is effective is deductible in the year the revocation is effective (subject to the requirements of any other provision under the Code, regulations, or any other published guidance) and the taxpayer will be required to amend any federal income tax returns affected by the revocation.

(d) *Effective date*. These regulations apply to a section 59(e) election made for a taxable year ending, or a request to revoke a section 59(e) election submitted, on or after December 22, 2004.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. In §602.101, paragraph (b) is amended by adding an entry in numerical order to the table to read as follows:

§602.101 OMB Control numbers.

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(b) * * *

CFR part or section where identified and described	Current OMB Control No.
* * * * *	
1.59–1	1545–1903
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Mark E. Matthews,
Deputy Commissioner for Services and Enforcement.

Approved December 15, 2004.

Gregory F. Jenner,
Acting Assistant Secretary of the Treasury (Tax Policy).

(Filed by the Office of the Federal Register on December 21, 2004, 8:45 a.m., and published in the issue of the Federal Register for December 22, 2004, 69 F.R. 76614)