



Tax and Accounting Center

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233 DTR G-1

Construction

Witnesses to Address IRS Severing Rules, Effective Date at Home Construction Hearing

Rich Shavell is expected to testify on behalf of Associated Builders and Contractors Inc. at a Dec. 5 Internal Revenue Service hearing that any new severing rules that may be issued should only apply to home construction contracts (HCCs) and should not supersede current regulations.

The proposed rules (REG-120844-07), issued Aug. 1, would expand the types of contracts that qualify for the home construction contract exemption and modify the rules for taxpayer-initiated changes in methods of accounting to comply with tax code Section 460 regulations (149 DTR G-1, 8/4/08).

In comments submitted to IRS from ABC, Shavell and Robert A. Hirsch, director of legal and regulatory affairs at ABC, wrote that the current severing rules apply to many other situations beside HCCs. Should revisions be made to the severing and completion rules that apply to general construction projects, small business contractors who meet the Section 460(e) exemption and use the completed contract method (CCM) would be negatively affected, they said.

ABC continues to seek a raise in the current Section 460(e) threshold of \$10 million, which has not been indexed for inflation since 1986 when the CCM was declared not an option for commercial contractors whose average annual gross receipts top that figure, Shavell and Hirsch wrote. ABC also stressed that it is opposed to any regulatory changes that would limit the construction contract exceptions to the percentage-of-completion method, they said.

Section 481(a) Adjustments.

Shavell and Hirsch wrote in their comments that the final regulations must explain the need for the proposed modifications to the handling of taxpayer-initiated changes. The proposed rules would continue the cutoff method of implementing taxpayer-initiated changes in methods of accounting, but only for changes from a permissible percentage-of-completion method (PCM) to another permissible PCM for long-term contracts for which PCM is required, and for taxpayer-initiated changes from one cost allocation method of accounting that complies with cost allocation rules to another, IRS said.

All other taxpayer-initiated changes in accounting method would be made with a Section 481(a) adjustment, IRS said in the proposed rules. Shavell and Hirsch wrote that it is unclear why the proposed rules require most of these changes to use a 481(a) adjustment when all taxpayer-initiated changes used to be handled with the cutoff method.

Shavell may testify that the final regulations should provide a transition period in which taxpayers can elect to use the cutoff method where it used to be available in the old rules so that they do not face any significant burden.

Levine to Testify About Effective Date.

Howard Levine of Roberts & Holland LLP, Washington, D.C., is expected to testify about the proposed rules' clarification that a condominium unit will be permitted to be treated as a separate building in order to determine whether the underlying contract qualifies as a home construction contract. No separate effective date has been provided for this change, Levine wrote in his comments. The modification is subject to the general effective date stipulated in the proposed rules, which is taxable years beginning after the date the rules are finalized, he said.

Therefore, the change would not be effective until taxable year 2010 at the earliest, Levine said. Levine asked in the comments that the modification be made effective for all open years in light of the current economic situation that condominium developers face.

Levine is also expected to urge IRS to issue a notice or revenue procedure as soon as possible allowing taxpayers to opt to use the PCM method or report sales of condominium units for all open years until the regulations are finalized. Such action would provide immediate relief to taxpayers experiencing difficulties due to the economic downturn, he wrote.

By Lauren Gardner

Texts of comments from Levine and Shavell are in TaxCore, along with comments from the Construction Financial Management Association, Grant Thornton LLP, and the Associated General Contractors of America. Additional comments are available for purchase from BNA PLUS at 800-372-1033 (select Option 5, then Option 2), or by e-mailing bnaplus@bna.com.

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