July 21, 2022

Mr. Scott Vance
Associate Chief Counsel
Income Tax & Accounting
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Revenue Procedure 2015-13, Changes in Methods of Accounting

Dear Mr. Vance:

The American Institute of CPAs (AICPA) recognizes and appreciates the significant volume of guidance that the Department of the Treasury ("Treasury") and the Internal Revenue Service (IRS) has issued related to Public Law 115-97, commonly referred to as the Tax Cuts and Jobs Act (TCJA or the "Act")[1] and other recent guidance. Prior to the TCJA, the AICPA provided a comment letter[2] with suggestions for revisions to Revenue Procedure 2015-13, *Changes in Methods of Accounting* (Rev. Proc. 2015-13) to achieve the goal of encouraging voluntary compliance with proper tax accounting methods.

The AICPA is pleased to submit additional comments with respect to the accounting method change procedures set forth in Rev. Proc. 2015-13. The AICPA has identified a number of items in Rev. Proc. 2015-13 that need to be updated in light of the TCJA and other recent guidance.

Our current suggestions include removal of references to the partnership technical termination rule, updates to reflect the new centralized partnership audit regime rules, updates to the eligible acquisition transaction election, clarification on the scope of the prior change within five years eligibility rule, and modifications to the audit protection rules for foreign corporations. The proposed revisions will provide clarity and encourage prompt voluntary compliance with the proper tax accounting method principles.

Specifically, the AICPA recommends that Treasury and the IRS provide modifications to the procedural rules in the following areas:

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[1] Public Law 115-97, 131 Stat. 2054.
[2] *See* AICPA Letter, "Re: 2015 Revenue Procedure 2015-13, Changes in Methods of Accounting," November 14, 2016.

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1. Transactions treated as the cessation of a trade or business

- Treasury and the IRS should remove section 3.04(2)(f) of Rev. Proc. 2015-13 to conform with the changes made by the TCJA.

2. Eligible acquisition transaction election

- Treasury and the IRS should remove the parenthetical reference to technical terminations from section 7.03(3)(d)(iii)(B) of Rev. Proc. 2015-13 to conform with the changes made by the TCJA.

3. Standard applied under Reg. §§ 301-9100-1 and 301.900-3 to the eligible acquisition transaction election

- Treasury and the IRS should apply the general standards under Treas. Reg. § 301.9100-3[3] (taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the government) in granting relief for a late eligible acquisition transaction election.

- Alternatively, if Treasury and the IRS continue to apply the unusual and compelling standard, Treasury and the IRS should distinguish between a "missed election" and the "perfection of an election" and also consider whether all affected taxpayers agreed to the election in evaluating whether the unusual and compelling standard is met rather than the factors considered for late accounting method changes.

4. Waiver of final year eligibility rule when five-year eligibility rule is waived for new guidance

- For new legislative or regulatory guidance, where the IRS has waived the five-year eligibility rule in section 5.01(1)(f) of Rev. Proc. 2015-13, the IRS should waive the final year eligibility rule in section 5.01(1)(d) of Rev. Proc. 2015-13 for the same period of time so that taxpayers may file a method change to comply with the legislative or regulatory guidance in the final year of a trade or business.

- In conjunction with this waiver, taxpayers applying the waiver of the eligibility rule in section 5.01(1)(d) of Rev. Proc. 2015-13 should also be required to accelerate the recognition of any section 481(a) adjustment such that it is recognized in its entirety for the year of change (i.e., the final year of the trade or business).

5. Scope of eligibility requirement that an accounting method change is not made or requested during the preceding five taxable years

[3] Unless otherwise indicated, all references are to the Internal Revenue Code of 1986, as amended, or to the Treasury Regulations promulgated thereunder.

- Treasury and the IRS should provide additional guidance, including examples under section 5.05 of Rev. Proc. 2015-13, to clarify the scope of the prohibition of changing the same item. Specifically, the automatic changes made under different Code sections should be considered separate items, and clarification that the last-in, first-out (LIFO) inventory submethod exception is an illustration of a change in submethods, and not an explicit exception to a prohibition on changes in submethods.

6. Exception from filing Form 3115, Application for Change in Accounting Method, for certain exempt organizations

- Treasury and the IRS should modify section 3.17 of Rev. Proc. 2015-13, which defines a "taxpayer" subject to the revenue procedure, to state that an exempt organization is not required to file a Form 3115 to make a change in accounting method for federal income tax purposes if it has no federal taxable income and no unrelated business income (UBI).

7. Partnerships under examination

- Treasury and the IRS should update section 3.18(3) of Rev. Proc. 2015-13 to reflect the new centralized partnership audit regime, referred to as the BBA examination rules (BBA).

8. Exception from audit protection for certain controlled foreign corporations or 10/50 corporations

- Consistent with our comments in our prior comment letter,[4] the IRS should delete section 3.08(4) of Rev. Proc. 2015-13 from the revenue procedure and apply the definitions applicable to domestic corporations in section 3.08(1) of Rev. Proc. 2015-13 to all taxpayers, including foreign corporations.

- In addition, the examination practice of sending general examination plans and information document requests (IDR) should be changed indicating that earnings and profits are reviewed during the examination.

- Also, the IRS should provide a third example in section 3.08(1) contrasting when an item is an issue under consideration for a foreign corporation and when it is not an issue under consideration, in a manner similar to the two examples already in this section.

- Furthermore, the IRS should restore a foreign corporation's ability to use the 120-day window to file an accounting method change when under exam.

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[4] *See* AICPA Letter, "Re: 2015 Revenue Procedure 2015-13, Changes in Methods of Accounting," November 14, 2016.

- Finally, the IRS should eliminate the 150 percent threshold restriction on receiving audit protection for foreign corporations.

BACKGROUND

Section 446(e) and the related regulations require that a taxpayer who changes its method of accounting on the basis of which the taxpayer regularly computes income in keeping its books must, before computing taxable income under the new method, secure the consent of the Commissioner of the IRS (Commissioner). Generally, a taxpayer must file a Form 3115, *Application for Change in Accounting Method*, to secure the Commissioner's consent to change a method of accounting.[5] Rev. Proc. 2015-13[6] provides the general procedures under section 446(e) and Treas. Reg. § 1.446-1(e) to obtain the consent of the Commissioner to change a method of accounting for federal income tax purposes. Specifically, it provides the general procedures to obtain the advance (non-automatic) consent of the Commissioner to change a method of accounting and provides the procedures to obtain the automatic consent of the Commissioner to change a method of accounting described in the List of Automatic Changes, currently contained in Rev. Proc. 2022-14, *List of Automatic Changes.*

SPECIFIC COMMENTS

1. Transactions treated as the cessation of a trade or business

Overview

One of the eligibility requirements for making both an automatic and non-automatic accounting method change is that the requested year of change is not the final year of the trade or business, subject to certain exceptions. Section 5.03(1) of Rev. Proc. 2015-13 provides that a taxpayer may not request the Commissioner's consent to make a change in method of accounting under Rev. Proc. 2015-13 for the taxable year the taxpayer ceases to engage in the trade or business to which the change in method of accounting would relate (final year), as defined in section 3.04 of Rev. Proc. 2015-13. Section 3.04(2) of Rev. Proc. 2015-13 provides examples of transactions that are treated as the cessation of a trade or business. One example, under section 3.04(2)(f) of Rev. Proc. 2015-13, provides that a cessation of a trade or business occurs when there is a sale or exchange of 50 percent or more of the total interest in a partnership's capital and profits under section 708(b)(1)(B) within a 12-month period.

Recommendation

The AICPA recommends that Treasury and the IRS remove section 3.04(2)(f) of Rev. Proc. 2015-13 to conform with the changes made by the TCJA.

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[5] Treas. Reg. § 1.446-1(e)(3)(i). The Commissioner may prescribe administrative procedures for a taxpayer to change its method not withstanding the requirement to secure the Commissioner's consent.

[6] 2015-5 I.R.B 419.

Analysis

The TCJA removed section 708(b)(1)(B), commonly known as a "technical termination." A partnership that met the requirements of a technical termination was considered to terminate, just as if it had actually terminated its business. Prior to the changes made by the TCJA, the inclusion of the technical termination rule in section 3.04(2)(f) of Rev. Proc. 2015-13 was consistent with section 708(b)(1)(B) and reinforced, and specifically applied the technical termination rule, to accounting method changes. However, because the TCJA removed the technical termination rule, section 3.04(2)(f) of Rev. Proc. 2015-13 should also be removed, which will eliminate confusion. Otherwise, taxpayers may not realize they are able to request the Commissioner's consent to make an accounting method change for the taxable year in which there is a sale or exchange of 50 percent or more of the total interest in a partnership's capital and profits within a 12-month period.

2. Eligible acquisition transaction election

Overview

A taxpayer that engages in an eligible acquisition transaction in the year it wishes to make an accounting method change, or in the subsequent taxable year on or before the due date, including extensions, for filing the federal income tax return for the year of change, may be able to make an election to include all of the positive section 481(a) adjustment in the year of change instead of recognizing the adjustment over four taxable years as generally required. An eligible acquisition transaction is described, in part, in section 7.03(3)(d)(iii)(B) of Rev. Proc. 2015-13 for taxpayers other than a controlled foreign corporation (CFC) or C corporation as "an acquisition of an ownership interest in the taxpayer by another party that does not cause the taxpayer to cease to exist for federal income tax purposes (for example, the sale or exchange of a partnership interest that does not cause a technical termination of the partner under section 708(b)(1)(B))."

Recommendations

The AICPA recommends that Treasury and the IRS remove the parenthetical reference to technical terminations from section 7.03(3)(d)(iii)(B) of Rev. Proc. 2015-13 to conform with the changes made by the TCJA.

In addition, consistent with our prior comment letter,[7] the AICPA recommends that the IRS allow taxpayers to elect to accelerate remaining positive section 481(a) adjustments related to accounting method changes made in prior years when an eligible acquisition transaction occurs.

Finally, to further align with the goal of allowing a target company or seller to bear the tax cost associated with its methods of accounting, the AICPA recommends that a taxpayer who elects

[7] *See* AICPA Letter, "Re: 2015 Revenue Procedure 2015-13, Changes in Methods of Accounting," November 14, 2016.

to accelerate its positive section 481(a) adjustment into its final pre-acquisition taxable year by making an eligible acquisition transaction election also be provided with a waiver of the restriction on making a change for the same item within the five taxable years ending with the year of change.

Analysis

As explained above, the TCJA removed the technical termination rule under section 708(b)(1)(B). Prior to the changes made by the TCJA, the inclusion of the technical termination rule in section 7.03(3)(d)(iii)(B) of Rev. Proc. 2015-13 was consistent with section 708(b)(1)(B) and useful in illustrating the definition of an eligible acquisition transaction. However, because the TCJA removed the technical termination rule, the parenthetical reference to the partnership technical termination rule should be removed from section 7.03(3)(d)(iii)(B) of Rev. Proc. 2015-13. Removing this section will eliminate confusion as the rule no longer exists and should no longer be used for illustrative purposes.

Further, under the eligible acquisition transaction election, a taxpayer is able to elect to accelerate all positive section 481(a) adjustments into the tax year of change, rather than spreading the positive adjustment over multiple (usually four) taxable years. This election simplifies the remediation of accounting methods issues identified during the due diligence process and allows the target company to bear the tax related to positive adjustments, which are commonly related to impermissible accounting methods identified as part of the due diligence process. These adjustments are corrected in the year prior to a transaction, or the year of a transaction. However, the process does not allow the acceleration of positive adjustments related to a change in method of accounting that the target company made more than a year before the transaction. Thus, under the current procedure, complicated indemnity provisions remain necessary in order to shift the tax burden from the buyer to the seller when the target company has positive section 481(a) adjustments from accounting method changes filed in prior years that are spread into post-transaction taxable years.

In addition, allowing a target company to elect to accelerate all remaining positive section 481(a) adjustments into the target company's final pre-acquisition taxable year would align with the goal of the current eligible acquisition transaction election, which allows the target company or seller to bear the tax cost associated with its methods of accounting. This modification also would avoid the need for complicated indemnity provisions in a transaction to shift the tax cost back to the seller.

Finally, allowing for a waiver of the restriction on making a change for the same item within the five taxable years ending with the year of change will align with the goal of allowing a target company or seller to bear the tax cost associated with its methods of accounting. For example, many taxpayers that have made accounting method changes to use accounting methods available to businesses having average annual gross receipts that do not exceed $25 million, adjusted for inflation, which are then subsequently acquired by a larger business, are required to make accounting method changes from the small business method(s). When the automatic accounting method change(s) that would normally be used to change from the small business method(s) does not waive the five taxable year restriction, the taxpayer is not able to make the accounting method change to the new required method(s) prior to the acquisition, and the need for complicated indemnity provisions to shift the tax cost back to the seller remains.

Rev. Proc. 2022-14 generally waives the prior five-year overall change restriction for a taxpayer making a change from the cash method in the first section 448 year, a mandatory section 448 year, or a mandatory section 447 year, as applicable; however, the taxpayer in the above example would want to change its overall method of accounting from cash to accrual in the tax year immediately preceding the acquisition. Accordingly, the five-year prior change restriction would not be waived in this case, since the year of change would not be a mandatory section 448 year as the taxpayer would not yet have surpassed the gross receipts or gross receipts plus ownership threshold.

3. Standard applied under Treas. Reg. §§ 301.9100-1 and 301.9100-3 to the eligible acquisition transaction election

Overview

Section 7.03(3)(d) of Rev. Proc. 2015-13 provides for the eligible acquisition transaction election, which permits a taxpayer to include the entire net positive section 481(a) adjustment into income in the tax year of change instead of spreading the adjustment over multiple (generally four) taxable years. Under section 6.03(4)(b) of Rev. Proc. 2015-13, except in unusual and compelling circumstances or as provided in section 6.03(4)(a) of Rev. Proc. 2015-13, a taxpayer is not eligible for an extension of time to make a late eligible acquisition transaction election under Treas. Reg. §§ 301.9100-1 and 301.9100-3. Because the election can only be made for a particular year, the unusual and compelling circumstances standard applied for accounting method changes is not the appropriate standard in granting relief for late eligible acquisition transaction elections.

Recommendation

The AICPA recommends that Treasury and the IRS apply the general standards under Treas. Reg. § 301.9100-3 (taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the government) in granting relief for a late eligible acquisition transaction election.

Alternatively, if Treasury and the IRS continue to apply the unusual and compelling standard, the AICPA recommends that Treasury and the IRS should distinguish between a “missed election” and the “perfection of an election” and also consider whether all affected taxpayers agreed to the election in evaluating whether the unusual and compelling standard is met rather than the factors considered for late accounting method changes.

Analysis

The eligible acquisition transaction election was first included in Rev. Proc. 2015-13. Prior to this election, if a target company used an impermissible method or was required to change its method as a result of the transaction, the impact of a positive section 481(a) adjustment would be borne in part by the purchaser. By making an eligible acquisition transaction election, the income and associated tax liability are more properly aligned and recognized by the target prior to the transaction. The general four-year spread of an unfavorable section 481(a) adjustment was intended to be favorable to taxpayers, including as an incentive to change to permissible accounting methods. The four-year spread period is a complicating factor in an acquisition context as material section 481(a) adjustments may require adjustments to purchase price or payments under tax indemnification provisions.

Under section 6.03(4)(b) of Rev. Proc. 2015-13, except in unusual and compelling circumstances or as provided in section 6.03(4)(a) of Rev. Proc. 2015-13, a taxpayer is not eligible for an extension of time to make a late eligible acquisition transaction election under Treas. Reg. §§ 301.9100-1 and 301.9100-3. The IRS imposes an unusual and compelling circumstances standard for relief with respect to accounting method changes because a change can be made in the current year with a "catch-up" adjustment that puts the taxpayer in the same position as if it had used the new method in prior years. That policy is inapplicable to the eligible acquisition transaction election, which impacts the spread of the section 481(a) adjustment as opposed to the year the method change is made.

The unusual and compelling standard is not appropriate for evaluating whether to grant section 9100 relief[8] for the failure to file the eligible acquisition transaction election statements due with the return and with the IRS national office. The policy of section 9100 relief is to permit taxpayers that are in reasonable compliance with the tax laws to minimize their tax liability by collecting from them only the amount of tax they would have paid if they had been fully informed and well advised.

The eligible acquisition transaction election is an election that can only be made for a particular tax year, unlike a method change, which generally may be for any tax year. Thus, the unusual and compelling standard is not the appropriate standard to apply in evaluating the grant of section 9100 relief for the eligible acquisition transaction election; rather, the general standards for granting relief under Treas. Reg. § 301.9100-3 (taxpayer acted reasonably and in good faith and granting relief will not prejudice the interests of the government) are the more appropriate standards for permitting a late eligible acquisition transaction election.

If the government were to continue to apply the unusual and compelling standard to a late or missed eligible acquisition transaction election, the government should consider factors of relevance to the election rather than applying its normal approach of only granting relief when the failure to make the election is due to intervening circumstances beyond the taxpayer's control. The AICPA believes that in applying the unusual and compelling circumstances

[8] The Treasury regulations offer a form of relief allowing a late election, commonly known as "section 9100 relief."

standard for an eligible acquisition transaction election, the government could distinguish between a "missed election" where the taxpayer was unaware of the election at the time the election was due and the "perfection of an election" where the taxpayer was fully aware of the election and related tax consequences, intended to make the election and filed its returns consistent with having made the election, but failed to satisfy one or more procedural steps for making the election. The government might also consider whether all affected taxpayers agreed to the election in evaluating whether to grant relief.

4. Waiver of final year eligibility rule when five-year eligibility rule is waived for new guidance

Overview

Section 3.04 of Rev. Proc. 2015-13 provides that a taxpayer is considered to cease to engage in a trade or business if the taxpayer terminates its existence, ceases operation of the trade or business, or transfers substantially all of the assets of the trade or business to another taxpayer. Section 5.03 of Rev. Proc. 2015-13 prohibits taxpayers from making a change in method of accounting for the taxable year the taxpayer ceases to engage in the trade or business to which the change in method of accounting would relate. While there is an exception for situations where the final year of the trade or business is due to a corporate reorganization to which section 381(a) applies, there is no exceptions for taxpayers that are engaging in an asset sale of a trade or business to another party.

As a result, taxpayers subject to new legislative or regulatory guidance are often unable to file a method change to comply with such guidance in the final year of a trade or business. For affected taxpayers, this restriction can leave the entity with lingering exposure in regard to its final tax return(s) as the taxpayer is essentially forced to file its final return using incorrect methods instead of the proper methods prescribed by the legislative or regulatory guidance. The inability to remediate this exposure can create business issues for taxpayers for which the final year of a trade or business is attributable to the sale of the trade or business to another party as there is no mechanism for the taxpayer to comply with the legislative or regulatory guidance prior to the sale transaction (unless the taxpayer has not filed its federal income tax return for the taxable year immediately preceding the sale transaction and qualifies to make an automatic accounting method change for that year).

Recommendation

For new legislative or regulatory guidance, where the IRS has waived the five-year eligibility rule in section 5.01(1)(f) of Rev. Proc. 2015-13, the AICPA recommends that the IRS waive the final year eligibility rule in section 5.01(1)(d) of Rev. Proc. 2015-13 for the same period of time so that taxpayers may file a method change to comply with the legislative or regulatory guidance in the final year of a trade or business.

In conjunction with this waiver, the AICPA recommends that taxpayers applying the waiver of the eligibility rule in section 5.01(1)(d) of Rev. Proc. 2015-13 also be required to accelerate the recognition of any section 481(a) adjustment such that it is recognized in its entirety for the year of change (i.e., the final year of the trade or business).

Analysis

The AICPA appreciates the government's historical concerns about method changes filed in the final year of a trade or business. However, the AICPA believes that a method change to apply new rules or regulations, for example the final § 1.451-3 regulations, presents a compelling case to provide an exception. Taxpayers should not be left with lingering exposure for a final tax return merely because the applicable tax regulations changed shortly before the business ended or the taxpayer ceased to exist.

For example, assume that calendar year Taxpayer A continued to apply the former income recognition rules under section 451 for its taxable years through 2019. For the 2020 taxable year, Taxpayer A intended to make a method change to apply the proposed § 1.451-3 regulations but ultimately had to defer making the method change due to budget constraints caused by the pandemic and intended to make the method change under the final § 1.451-3 regulations for its 2021 taxable year instead. On October 31, 2021, Taxpayer A sold all of the assets of its trade or business to another party. As a result, the short taxable period ended October 31, 2021, is the final year of Taxpayer A's trade or business under section 3.04 of Rev. Proc. 2015-13. Under the AICPA's recommendation, Taxpayer A would be allowed to request to change to the final § 1.451-3 regulations for the taxable year ended October 31, 2021. However, Taxpayer A's section 481(a) adjustment computed as of January 1, 2021, would be recognized in its entirety during the taxable year ended October 31, 2021.

5. Scope of eligibility requirement that an accounting method change is not made or requested during the preceding five taxable years

Overview

Sections 5.01(1)(f) and 5.05 of Rev. Proc. 2015-13 generally prevent a taxpayer from making an automatic accounting method change if the taxpayer has made or requested a change for the same item during any of the five taxable years ending with the year of change. In many cases, clarity is needed in terms of what the "same item" is and how similar the later method change is to the earlier method change in order to determine if the five-year rule applies.

Recommendation

The AICPA requests additional guidance, including examples under section 5.05 of Rev. Proc. 2015-13, to clarify the scope of the prohibition of changing the same item. Specifically, the AICPA recommends that automatic changes made under different Code sections are considered separate items, and clarification that the last-in, first-out (LIFO) inventory submethod exception is an illustration of a change in submethods, and not an explicit exception to a prohibition on changes in submethods.

Analysis

Section 5.05 of Rev. Proc. 2015-13 provides that, if during any of the five taxable years ending with the year of change a taxpayer changed, or applied for consent to change, its method of accounting for a specific item, regardless of whether it implemented that change, the taxpayer may not request the Commissioner's consent to change its method of accounting for that same item under the automatic change procedures.

In many cases, it is not clear what is considered to be the same item, or whether making a second change using the same designated automatic accounting method change number (DCN) triggers this prohibition. Additionally, it is not clear how this rule may apply to submethods of accounting, other than the examples provided, which only discuss LIFO inventory submethods.

The following questions and proposed answers circumscribe our understanding of the intended scope of the five-year rule:

1. Is the later method change a reversal of the exact same earlier method change?

    a. An example is an initial method change under the LIFO method from the earliest acquisitions cost method to the latest acquisitions cost method, followed by a method change back to the earliest acquisitions cost method within the five-year period.

    b. This is the type of situation targeted by the five-year rule and is an appropriate type of situation in which to apply the five-year rule.

2. Does the later method change involve the same item as the earlier method change, but the later method change does not reverse the earlier method change?

    a. An example is an initial method change under the LIFO method from the earliest acquisitions cost method to the latest acquisitions cost method, followed by a method change from the latest acquisitions cost method to the average acquisitions cost method within the five-year period.

    b. The IRS may consider this situation as one under which the taxpayer is prohibited from making the second change within the five-year period, but the policy reasons underlying the potential disallowance of the second automatic change are not clear. Although both method changes relate to determining the current year cost under the LIFO method, it is unclear what policy is served by applying the five-year rule in this type of situation.

3. Does the later method change involve the same class of item as the earlier method change, or the exact same item as the earlier method change?

a. An example is a change to capitalize facilitative transaction costs in merger X, whereas the later method change is to capitalize facilitative costs in merger Y. The class of items is facilitative transaction costs in all mergers.

b. A second example is an accounting method change for a producer to use the modified simplified production method under section 263A without using the 5 percent de minimis rule for certain direct material costs, and then a later method change to use the 5 percent de minimis rule for certain direct material costs.

c. We believe the IRS should not consider these situations as ones under which the taxpayer is prohibited from making the second change within the five-year period because the specific items in the second change were not included in the first change. It is unclear what policy would be served by applying the five-year rule in these types of situations. Although the items are in the same general category (e.g., facilitative transaction costs under section 263(a) or costs subject to section 263A), the specific items being changed in each accounting method change are different so they should not be considered the "same item."

4. Does the later method change involve a different class of items than the class of items in the earlier method change, but the later method change is still within the same DCN?

   a. An example is a change under Treas. Reg. § 1.263(a)-4 to capitalize the costs of acquiring multi-year licenses where the costs were previously deducted, whereas the later method change involves the capitalization of investigatory merger costs in merger transactions under Treas. Reg. § 1.263(a)-5, where those merger costs were previously deducted. While the two method change items are obviously dissimilar, the changes are under the same DCN.

   b. It is unclear whether the IRS would preclude the second automatic change in this type of case, but the later method change of this type should be eligible to be made under the automatic procedures. Although under the same DCN, the item being changed is different and should not be precluded under the five-year rule.

5. Some automatic accounting method changes appear to waive the five-year rule for changes in the same item based on the order in which the changes occur, and it is not clear what the policy reason is for waiving the five-year rule based on the ordering of the changes.

   a. For example, with respect to the automatic change from an impermissible to permissible method of accounting for depreciation or amortization, section 6.01(2) of Rev. Proc. 2022-14 waives the five-year rule if in the prior five years, a taxpayer requested or made a change in method of accounting from expensing to capitalizing, or vice versa, the cost or other basis of an asset. However, under section 11.08 of Rev. Proc. 2022-14, which provides an automatic change for tangible property, including changes to deduct amounts incurred for repair and maintenance and a change to capitalize amounts paid or incurred for improvements to tangible property, the five-year rule is not waived.

b. In this example, the IRS likely considers that the item is the same for each of the changes, otherwise, there is no need to specifically waive the five-year rule for the depreciation accounting method change. The order in which the changes occur impacts whether the five-year rule is applicable, however, it is unclear what policy is served by applying the five-year rule selectively based on the ordering of the method changes.

6. Exemption from filing Form 3115 for certain exempt organizations

Overview

There has long been confusion and discussion about the need or usefulness for an exempt organization with no federal taxable income and unrelated business income (UBI) to file a Form 3115 to change its accounting method. Rev. Proc. 2022-5, *Determination Letters*, *Exempt Organizations,* has clarified situations under which an exempt organization does not have to file Form 3115.

Recommendation

The AICPA recommends that section 3.17 of Rev. Proc. 2015-13, which defines a "taxpayer" subject to the revenue procedure, is modified to state that an exempt organization is not required to file a Form 3115 to make a change in accounting method for federal income tax purposes if it has no federal taxable income and no UBI.

Analysis

Rev. Proc. 2022-5, which provides procedures for issuing determination letters on issues under the jurisdiction of the Director, Exempt Organizations (EO) Rulings and Agreements, added section 2.03(1) to the prior year version of the revenue procedure to explain how a tax-exempt organization may change its method of accounting. Specifically, section 2.03(1) of Rev. Proc. 2022-5 states that:

> (1) **"Form 3115, Application for Change in Accounting Method**. A tax-exempt organization described in section 501(c) that wants to change its method of accounting for computing taxable income must follow the procedures that are generally applicable to all taxpayers for requesting the Commissioner's consent to an accounting method change, including, if applicable, filing a Form 3115, *Application for Change in Accounting Method* (see, *e.g*., Rev. Proc. 2015-13, 2015-5 I.R.B. 419, as modified and clarified by Rev. Proc. 2021-34, 2021-35 IRB 337 (or any successor)). A tax-exempt organization described in section 501(c) must request consent to change its method of accounting for computing taxable income only if the tax-exempt organization has previously adopted a method of accounting for computing taxable income for the item(s) being changed. A taxpayer

> generally adopts a method of accounting in the first year in which an item is taken into account in computing taxable income. Thus, a tax-exempt organization that has adopted a method of accounting for an item of income or expense from an unrelated trade or business must generally request consent in order to change its method of accounting for reporting the item in any subsequent year, regardless of whether the gross income from the unrelated trade or business is greater than or equal to $1,000 in such subsequent year. However, a tax-exempt organization that has not yet adopted a method of accounting for an item does not have to request consent to change the methodology of reporting the item. Thus, a tax-exempt organization that is required to file a Form 990-T, *Exempt Organization Business Income Tax Return (and proxy tax under section 6033(e))* solely due to owing a section 6033(e)(2) proxy tax but has not yet adopted a method of accounting for an item of income or expense does not have to request consent to change its methodology for reporting such item on its Form 990-T (or Form 990, as applicable). See Rev. Proc. 2015-13, as modified and clarified by Rev. Proc. 2021-34, and Section 9 of Rev. Proc. 2022-1, this Bulletin for procedures applicable to taxpayers, including tax-exempt organizations, for requesting changes in method of accounting."

There is no accounting method guidance that states that an organization with no federal taxable income or UBI does not need to file an accounting method change. Section 3.17 of Rev. Proc. 2015-13 should be modified to reflect the language in section 2.03(1) of Rev. Proc. 2022-5, similar to the following: "A tax-exempt organization described in section 501(c) must request consent to change its method of accounting for computing taxable income only if the tax-exempt organization has previously adopted a method of accounting for computing taxable income for the item(s) being changed. A taxpayer generally adopts a method of accounting in the first year in which an item is taken into account in computing taxable income. Thus, a tax-exempt organization that has adopted a method of accounting for an item of income or expense from an unrelated trade or business must generally request consent in order to change its method of accounting for reporting the item in any subsequent year. However, a tax-exempt organization that has not yet adopted a method of accounting for an item does not have to request consent to change the methodology of reporting the item. Thus, a tax-exempt organization that is required to file a Form 990-T solely due to owing a section 6033(e)(2) proxy tax but has not yet adopted a method of accounting for an item of income or expense does not have to request consent to change its methodology for reporting such item on its Form 990-T (or Form 990, as applicable)."

Updating Rev. Proc. 2015-13 to state this position will reach a wider audience to make more practitioners aware of this position, and reduce time and money spent by organizations and their advisors that may not think to turn to the exempt organization determination letter procedural guidance in evaluating whether an accounting method change needs to be filed.

7. Partnerships under examination

<u>Overview</u>

A taxpayer may file an accounting method change under Rev. Proc. 2015-13 even if it is under examination at the time it files its application with IRS. However, unless it meets certain exceptions, a taxpayer would not receive audit protection (meaning, the IRS may require the taxpayer to change its method of accounting for the same item for a taxable year prior to the requested year of change). Section 3.18 of Rev. Proc. 2015-13 provides rules as to when a taxpayer will be considered under examination with respect to a federal income tax return and when an examination will end for accounting method change purposes. Section 3.18(3) of Rev. Proc. 2015-13 describes these rules for a partnership subject to the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), which were the procedures in effect when Rev. Proc. 2015-13 was issued.

Recommendation

The AICPA recommends that section 3.18(3) of Rev. Proc. 2015-13 be updated to reflect the new centralized partnership audit regime, referred to as the BBA examination rules (BBA).

Analysis

The BBA was enacted under Public Law No. 114-74, the Bipartisan Budget Act of 2015. The BBA is a new statutory regime for auditing, adjusting, assessing, and collecting tax from all partnerships, and replaces the TEFRA rules. It is effective for tax years beginning on or after January 1, 2018.

Section 3.18(3) of Rev. Proc. 2015-13 should be updated to indicate that a partnership subject to BBA is under examination as of the date of the notice of administrative proceeding that is sent to the partnership and partnership representative (Letters 5893 and 5893-A). Further, it should be updated to indicate that an examination ends:

(a) In a case in which the IRS accepts the partnership return as filed, on the date of the "no adjustments" final letter or the "no change" notice of final partnership adjustment that is sent to the partnership representative;

(b) In a fully agreed case, the date the partnership representative indicates agreement with the adjustments by executing Letters 5933 and 5933-A, the partnership generally must either pay an imputed underpayment based on the adjustments or elect to "push out" the adjustments to reviewed year partners. If the partnership pays imputed underpayment, any adjustments that do not result in an imputed underpayment is taken into account by the partnership in the adjustment year. A partnership that elects to push out must complete and execute the Form 8985, Pass-Through Statement – Transmittal/Partnership Adjustment Tracking Report and furnish Form 8986, Partner's Share of Adjustment(s) to Partnership-Related Item(s) to its reviewed year partners;[9] or

[9] *See* IRS BBA Partnership Audit Process guide for further information and process(es).

(c) In an unagreed or a partially agreed case, on the earliest of the date the IRS notifies the partnership representative that the examining agent(s) has transferred jurisdiction for the case to Appeals (for example, the date that Appeals issues its uniform acknowledgement letter to the partnership representative), the date the partnership representative requests judicial review, or the date of which the period for requesting judicial review expires.

8. Exception from audit protection for certain controlled foreign corporations or 10/50 corporations

Overview

Rev. Proc. 2015-13 contains several provisions that make it more difficult for controlled foreign corporations or 10/50 corporations (collectively "foreign corporations") to make an accounting method change when they or their controlling domestic shareholders are under examination. As explained in more detail below, section 3.08(4) of Rev. Proc. 2015-13 provides a broad definition of "issue under consideration" for a foreign corporation, section 8.02(1)(b)(iii) of Rev. Proc. 2015-13 prohibits a foreign corporation under exam from filing an accounting method change within the 120-day window, and section 8.02(5) of Rev. Proc. 2015-13 contains a "150 percent threshold," which limits a foreign corporation's ability to receive audit protection.

Recommendations

Consistent with our comments in our prior comment letter,[10] the AICPA recommends that the IRS delete section 3.08(4) of Rev. Proc. 2015-13 from the revenue procedure and apply the definitions applicable to domestic corporations in section 3.08(1) of Rev. Proc. 2015-13 to all taxpayers, including foreign corporations.

In addition, the AICPA recommends changing the examination practice of sending general examination plans and information document requests (IDR) indicating that earnings and profits are reviewed during the examination.

Also, the AICPA recommends that the IRS provide a third example in section 3.08(1) contrasting when an item is an issue under consideration for a foreign corporation and when it is not an issue under consideration, in a manner similar to the two examples already in this section.

Furthermore, the AICPA recommends that the IRS restore a foreign corporation's ability to use the 120-day window to file an accounting method change when under exam.

Finally, the AICPA requests that the IRS eliminate the 150 percent threshold restriction on receiving audit protection for foreign corporations.

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[10] *See* AICPA Letter, "Re: 2015 Revenue Procedure 2015-13, Changes in Methods of Accounting," November 14, 2016.

Analysis

Section 3.08(4) of Rev. Proc. 2015-13 states "in the case of a CFC or 10/50 corporation, the foreign corporation's method of accounting for an item is an issue under consideration if any of the corporation's controlling domestic shareholders (as defined in §1.964-1(c)(5)) receives notification described in section 3.08(1), 3.08(2), or 3.08(3) that the treatment of a distribution, deemed distribution, or inclusion from the foreign corporation, or the amount of its earnings and profits or foreign taxes deemed paid, is an issue under consideration."

Under this "broad" definition of issue under consideration, a foreign corporation's method of accounting is an issue under consideration if any of the corporation's controlling domestic shareholders receive notification (i.e., by draft or final examination plan, information document request (IDR), notice of proposed adjustment or income tax examination changes) from the examining agent that "*the treatment of a distribution, deemed distribution, or inclusion from the foreign corporation, or the amount of its earnings and profits or foreign taxes deemed paid, is an issue under consideration*" [Emphasis added]. Thus, under this broad definition, *all* of the methods of accounting used to compute earnings and profits are under consideration if the controlling domestic shareholder(s) has received notice that the earnings and profits of the foreign corporation is an issue under consideration. This definition is the equivalent to treating all of the methods of a domestic corporation as being under consideration if the taxpayer receives notification that the IRS is auditing taxable income.

In contrast, the term issue under consideration in the narrow sense, as defined for a domestic entity in section 3.08(1) of Rev. Proc. 2015-13, means a taxpayer's method of accounting for an item is an issue under consideration for the taxable years under examination as of the date of any written notification to the taxpayer (for example, by draft or final examination plan, IDR, or notification of proposed adjustments or income tax examination changes) from the examining agent(s) "*specifically citing the treatment of the item as an issue under consideration*" [Emphasis added]. Under Rev. Proc. 2015-13, the concept of the "narrow" definition of issue under consideration applicable to domestic corporations is applicable to foreign corporations *only* after the foreign corporation has been under examination and had an issue under consideration in the broad sense for 24 months.

In many examinations of U.S. multinational corporations, a taxpayer is notified in an examination plan or in an initial-round IDR that the amount of the earnings and profits or deemed paid taxes of its foreign corporations is an issue under consideration. The experience of our membership is consistent with the Internal Revenue Manual (I.R.M) provisions related to examinations of CFCs. Section 4.61.7.39 of the I.R.M provides that "[t]he proper determination of earnings and profits is *vital* in the examination of a CFC [Emphasis added]." Further, section 4.61.7.40 of the I.R.M provides earnings and profit guidelines, the first of which is: "[d]etermine that the proper books and records were used to compute the profit and loss statement from which the determination of earnings and profits was calculated."

Given this guidance in the I.R.M for the examination process of a CFC, it is difficult to imagine an examination where the controlling domestic shareholder is not notified early in the process that the earnings and profits of its foreign corporations is an issue under consideration. Thus, in the examination of many U.S. multinational corporations, it is not uncommon for all of a foreign corporation's methods to be considered under consideration in the broad sense of the term. The fact that Rev. Proc. 2015-13 allows changes when the issue is under consideration in the broad sense for 24 months and not when the issue is under consideration in the narrow sense does little to mitigate our concerns. In light of the audit currency initiative of the IRS, many foreign corporations do not have issues under consideration in the broad sense for 24 months, particularly considering the new rule that issues under consideration close when the examination closes. This fact, combined with the elimination of the 120-day window, effectively makes it impossible for many foreign corporations to voluntarily change from improper methods with a positive section 481(a) adjustment and seems inconsistent with the longstanding policy of encouraging voluntary self-reporting and self-remediation of impermissible accounting methods.

Changing the examination practice of sending general examination plans and IDRs indicating that earnings and profits are reviewed during the examination will help provide opportunities for foreign corporation to file an accounting method change.

In addition, providing a third example in section 3.08(1) of Rev. Proc. 2015-13 contrasting when an item is an issue under consideration for a foreign corporation and when it is not an issue under consideration, in a manner similar to the two examples already in this section, will help for clarification.

The restrictions in the three-month window period in Rev. Proc. 2015-13 regarding issues under consideration for foreign corporations raise additional concerns. Under the three-month window for foreign corporations, a foreign corporation, or the designated shareholder of a foreign corporation, may file an application for a change in method of accounting during the three-month window if all of its controlling domestic shareholders that are under examination have been under examination for at least 24 consecutive months as of the first day of the three-month window (as opposed to 12 consecutive months for domestic entities). The three-month window is available only if the method of accounting that the foreign corporation is seeking to change is either not an issue under consideration (in the "broad" sense) in an examination, before an appeals office, or before a federal court as of the date the designated shareholder files the Form 3115, or has been an issue under consideration (in the "broad" sense) for at least 24 consecutive months as of the date the designated shareholder files the Form 3115, and is not yet an issue under consideration in the "narrow" sense.[11]

As a result of the significant restrictions on the ability to use the three-month window period, the definition of the term issue under consideration for foreign corporations contained in the revenue procedure prevents voluntary compliance with proper accounting methods. For a foreign corporation that is under examination and seeking to change an impermissible method with a positive section 481(a) adjustment, the limited availability of the three-month window essentially precludes it from changing to a permissible method and obtaining audit protection. As a consequence, foreign corporations are forced to remain on their impermissible methods of

[11] Rev. Proc. 2015-13, section 8.02(1)(a)(iii).

accounting, to change their method without filing a Form 3115, or to file an accounting method change without audit protection. None of these options are in the best interest of sound tax administration.

The rationale for the broad definition of issue under consideration may have resulted from the examination practice of issuing general IDRs to audit the earnings and profits of a foreign corporation, as opposed to specific IDRs citing specific methods for examination. Rather than frustrating voluntary compliance for foreign corporations, more efficient administration of the tax law results from allowing and encouraging voluntary compliance with proper tax accounting principles, by aligning the definition of an issue under consideration for foreign corporations with the definition for domestic corporations.

To address the concern that the alignment of definitions would lead to no issues under consideration for a foreign corporation, Treasury and the IRS should change the examination practice of sending general examination plans and IDRs indicating that earnings and profits are reviewed during the examination. The IRS should instruct examining agents to conduct examinations of foreign corporations' earnings and profits in a manner comparable to the examinations of domestic corporations' taxable income, that is, with narrowly targeted examination plans and IDRs. This examination practice would eliminate all-encompassing examination plans and IDRs that would render every accounting method issue that is raised in respect of earnings and profits of a foreign corporation as an issue under consideration. Only those foreign corporations with specifically identified items being examined in respect of their earnings and profits would be appropriately precluded from utilizing the three-month window for method changes related to such items, consistent with the treatment of domestic corporations.

The tax policy behind Rev. Proc. 2015-13 is to encourage voluntary compliance by providing favorable terms and conditions for a taxpayer-initiated method change. Section 1.02 of Rev. Proc. 97-27,[12] the predecessor to Rev. Proc. 2015-13, explained that the goal of the voluntary method change procedures is to provide "incentives to encourage prompt voluntary compliance with proper tax accounting principles," presumably because voluntary compliance generally is accepted as the most efficient manner of administering the tax law. Thus, Rev. Proc. 97-27 provided incentives for voluntary compliance similar to those provided in Rev. Proc. 2015-13, including a choice of permissible methods, a current year of change, a four-year spread of an unfavorable section 481(a) adjustment, and, in most cases, audit protection preventing the IRS from raising the same issue in an earlier taxable year. These incentives contrast sharply with the consequences of a change made as part of an examination. With an IRS-initiated method change, the IRS generally changes to a method that in its opinion clearly reflects income, makes the change effective for the earliest taxable year under examination, and allows no spread for the unfavorable section 481(a) adjustment. The broad definition of issue under consideration for foreign corporations is inconsistent with tax policy underlying Rev. Proc. 2015-13 of providing incentives for voluntary compliance because foreign corporations under examination are often precluded from using the exceptions to voluntarily change from an impermissible method with a positive section 481(a) adjustment.

[12] 1997-2 C.B. 680.

Finally, the definition of issue under consideration for foreign corporations is inconsistent with congressional intent, as expressed in section 964 as well as the regulations promulgated thereunder. These provisions reflect an intent to treat foreign corporations in a manner substantially similar to domestic corporations in respect of accounting methods for earnings and profits. Under section 964, earnings and profits and any deficit in earnings and profits of a foreign corporation is determined under rules "substantially similar" to those applicable to domestic corporations. The regulations promulgated under section 964 require that the methods of accounting for earnings and profits of a foreign corporation reflect the provisions of section 446. Thus, generally foreign corporations are subject to the accounting methods procedural rules applicable to domestic corporations. The special procedural rule applicable to foreign corporations for determining when an issue is under consideration , which contrasts with the rule applicable to domestic corporations, is inconsistent with the intent of section 964 to treat foreign corporations similar to domestic corporations.

Section 8.02(1)(b) of Rev. Proc. 2015-13 permits a taxpayer that files an accounting method change in the 120-day period following the date an examination of the taxpayer ends, regardless of whether a subsequent examination has commenced, to receive audit protection for the change. However, under section 8.02(1)(b)(iii) of Rev. Proc. 2015-13, the 120-day window provisions are not available for a foreign corporation. Taxpayers under examination that are changing from impermissible accounting methods with positive section 481(a) adjustments generally will seek to file their method change applications within the three-month or 120-day window in order to obtain audit protection. Taxpayers changing from impermissible methods generally seek audit protection to avoid interest and penalties, as well as additional complexities arising if the IRS raises the same issue as part of an examination of an earlier tax year. Thus, availability of the three-month and 120-day windows is critical for a taxpayer with a positive section 481(a) adjustment to voluntarily change from an impermissible method.

Due to the restrictions for a foreign corporation to file in the three-month window, as discussed above, the 120-day window would be the only reasonable mechanism for a foreign corporation under IRS examination to voluntarily change from an improper method with a positive section 481(a) adjustment and obtain the same favorable terms and conditions applicable to domestic corporations. Rev. Proc. 2015-13 specifically states that IDRs remain issues under consideration until the examination closes. Therefore, due to the broad definition of issue under consideration, the 120-day window would provide the only option for most foreign corporations under IRS examination to change from an impermissible method. The elimination of the 120-day window combined with the rule that IDRs remain issues under consideration until the examination closes are serious impediments to a foreign corporation's ability to correct an impermissible method. The AICPA believes that the 120-day window remains a critical opportunity for a foreign corporation to make an accounting method change to correct an impermissible accounting method with a positive section 481(a) adjustment and obtain audit protection. The AICPA does not believe there are any strong policy concerns to deny use of the 120-day window for foreign corporations.

Section 8.02(5) of Rev. Proc. 2015-13 provides that:

> "In the case of a change in method of accounting made on behalf of a CFC or 10/50 corporation, the IRS may change the method of accounting for the same item that is the subject of a Form 3115 filed under this revenue procedure for taxable years prior to the requested year of change in which any of the CFC or 10/50 corporation's domestic corporate shareholders computed an amount of foreign taxes deemed paid under sections 902 and 960 with respect to the CFC or 10/50 corporation that exceeds 150 percent of the average amount of foreign taxes deemed paid under sections 902 and 960 by the domestic corporate shareholder with respect to the CFC or 10/50 corporation in the shareholder's three prior taxable years."

Because this provision effectively overrides other exceptions that provide no audit protection under section 8.02 of Rev. Proc. 2015-13, it is a trap for taxpayers. For a foreign corporation, whether it is under examination or not, seeking to change an impermissible method with a positive section 481(a) adjustment, this exception essentially precludes it from changing to a permissible method and obtaining audit protection. As a consequence, foreign corporations are forced to remain on their impermissible methods of accounting, to change their method without filing a Form 3115, or to file an accounting method change without audit protection. The AICPA believes that none of these options are in the best interest of sound tax administration.

In addition, under GILTI (section 951A), the earnings of a CFC are taxed each year, similar to any domestic corporation, and unlike E&P which generally was only taxed if there was a distribution or other recognition transaction. As a CFC's earnings are taxed each year, there is no need for a special rule for CFCs with respect to the accumulation of their earnings and therefore the 150 percent threshold is not necessary.

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We appreciate your consideration of our recommendations and welcome the opportunity to further discuss our comments. If you have any questions, please contact David Strong, Chair, AICPA Tax Methods and Periods Technical Resource Panel, at (616) 752-4251, or david.strong@crowe.com; or Elizabeth Young, Senior Manager — AICPA Tax Policy & Advocacy, at (202) 434-9247, or elizabeth.young@aicpa-cima.com; or me at (601) 326-7119 or JanLewis@HaddoxReid.com.

Sincerely,

Jan Lewis, CPA
Chair, AICPA Tax Executive Committee

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