

Repairs & Capitalization Guidelines
Small Businesses without Audited Financial Statements
Presented By David A. Reumont CPA PC

Step 1: Adopt the Capitalization Policy - De Minimis Safe Harbor Policy and procedures

Step 2: Materials, supplies, equipment and repairs - apply De Minimis and safe harbor maintenance rules as follows:

- a. Charge as an expense supplies and maintenance items lasting less than 12 months;
- b. Charge as an expense all supplies and maintenance items costing less than \$200.00.
- c. Charge as an expense equipment, repairs and acquisitions costing less than \$500 per policy.
- d. Charge as an expenses repair items, which replace or are expected to replace items in a unit of property more than once during asset life.

Step 3: Buildings (Residential or Commercial) - apply safe harbor maintenance rules as follows:

- a. Expense items replaced or expected to be replaced within a 10-year period;
- b. Determine if qualified small business with revenues less than \$10,000,000;
- c. Determine if building original cost is less than \$1,000,000;
- d. If both b and c are met, determine if total maintenance costs including other current year expense items are less then \$10,000 per building
- e. If d is met, expense the amounts; otherwise apply the capitalization rules below.

Step 4: Determine the Unit of property;

Step 5: Apply the three Betterment tests to each item, whose individual cost is greater than \$500:

1. Does the expense ameliorate a condition or defect from before acquisition or during its production or ownership?
2. Is the expense a material addition, enlargement or expansion of a Unit of Property?
3. Does the expense materially increase the output, capacity, quality, etc. of the Unit of Property?

If any one applies then capitalize the cost, if none of these betterment tests apply, then go to Step 6.

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Step 6: Apply the five restoration tests to each item whose individual costs is greater than \$500:

1. Does the expense replace a component previously deducted?
2. Does the expense repair a component after a casualty?
3. Does the expense return a component to operating condition from a condition of nonfunctioning disrepair?
4. Does the expense rebuild a component after the end of its tax life?
5. Does the expense replace a part or combination of parts of a major component or structure?

If any one applies you must capitalize the cost, otherwise go to Step 7.

Step 7: Apply the two-adaption tests to each item, whose individual cost is greater than \$500:

1. Does the expense allow the Unit of Property to be used in a new use?
2. Does the expense allow the Unit of Property to be used in a different use?

If any one under step 7 applies, then capitalize the cost.

These summarized steps are for guidance in how the new rules apply to small businesses without audited financial statements and who elect to use the de minimis safe harbor election. These rules are extremely complex and detailed under Internal Revenue Service Guidelines and Regulations.

Please consult with David A. Reumont CPA PC in using this Guideline.