

Part III

Administrative, Procedural, and Miscellaneous

26 CFR 601.204: Changes in accounting periods and in methods of accounting.

(Also, Part 1, §§ 174, 446, 1.446-1.)

Rev. Proc. 2023-8

SECTION 1. PURPOSE

This revenue procedure modifies Rev. Proc. 2022-14, 2022-7 I.R.B. 502, to provide procedures under § 446 of the Internal Revenue Code (Code) and § 1.446-1(e) of the Income Tax Regulations to obtain automatic consent of the Commissioner of Internal Revenue (Commissioner) to change methods of accounting for specified research or experimental expenditures to comply with § 174 of the Code, as amended by § 13206 of Public Law 115-97, 131 Stat. 2054 (December 22, 2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA). References in this revenue procedure to “former § 174” refer to § 174 as in effect for research or experimental expenditures paid or incurred in taxable years beginning before the effective date of the amendments made to § 174 by § 13206(a) of the TCJA, and all following references to “§ 174” in this revenue procedure refer to § 174 as amended by the TCJA.

SECTION 2. BACKGROUND

.01 Former § 174.

(1) Former § 174(a)(1) provided that a taxpayer may treat research or experimental expenditures which are paid or incurred by the taxpayer during the taxable year in connection with the taxpayer's trade or business as expenses which are not chargeable to capital account. The expenditures so treated were allowed as a deduction. Under former § 174(a)(2)(A), a taxpayer could, without the consent of the Secretary of the Treasury or her delegate (Secretary), adopt the method provided in former § 174(a) for the taxpayer's first taxable year for which expenditures described in former § 174(a)(1) were paid or incurred. Under former § 174(a)(2)(B), a taxpayer could, with the consent of the Secretary, adopt at any time the method provided in former § 174(a).

(2) Under former § 174(b)(1), at the election of the taxpayer, made in accordance with regulations prescribed by the Secretary, research or experimental expenditures could be treated as deferred expenses if such expenditures were: 1) paid or incurred by the taxpayer in connection with the taxpayer's trade or business, 2) not treated as expenses under former § 174(a), and 3) chargeable to capital account but not chargeable to property of a character which is subject to the allowance under § 167 of the Code (relating to allowance for depreciation, etc.) or § 611 of the Code (relating to allowance for depletion).

(3) Former § 174(b)(1) provided that in computing taxable income, such deferred expenses were allowed as a deduction ratably over such period of not less than 60 months as may be selected by the taxpayer (beginning with the month in which the taxpayer first realizes benefits from such expenditures). Such deferred expenses were

expenditures properly chargeable to capital account for purposes of § 1016(a)(1) of the Code (relating to adjustments to basis of property).

(4) Under former § 174(b)(2), the election provided by former § 174(b)(1) could be made for any taxable year, but only if made not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof). The method so elected, and the period selected by the taxpayer, were required to be adhered to in computing taxable income for the taxable year for which the election was made and for all subsequent taxable years unless, with the approval of the Secretary, a change to a different method (or to a different period) was authorized with respect to part or all of such expenditures. The election did not apply to any expenditure paid or incurred during any taxable year before the taxable year for which the taxpayer made the election.

(5) Under § 1.174-1, which applies to research or experimental expenditures paid or incurred in taxable years beginning before December 31, 2021 (the effective date of the amendments to § 174 under § 13206 of the TCJA), research or experimental expenditures which are neither treated as expenses nor deferred and amortized under § 174 must be charged to capital account.¹

.02 TCJA amendments.

(1) As amended by § 13206(a) of the TCJA, § 174(a)(1) provides that in the case of a taxpayer's specified research or experimental expenditures for any taxable year, except as provided in § 174(a)(2), no deduction is allowed for such expenditures.

¹ The term "capital account" in § 1.174-1 includes capital asset accounts, including, but not limited to, inventory and depreciable property.

Section 174(a)(2) provides that the taxpayer must charge such expenditures to capital account² and is allowed an amortization deduction of such expenditures ratably over the 5-year period (15-year period in the case of any specified research or experimental expenditures which are attributable to foreign research within the meaning of § 41(d)(4)(F) of the Code) beginning with the midpoint of the taxable year in which such expenditures are paid or incurred. The method of accounting described in this section 2.02(1) is referred to as the “required § 174 method” in this revenue procedure.

(2) Under § 174(b) the term “specified research or experimental expenditures” means, with respect to any taxable year, research or experimental expenditures which are paid or incurred by the taxpayer during such taxable year in connection with the taxpayer's trade or business.

(3) Section 174(c)(1) provides that the required § 174 method does not apply to any expenditure for the acquisition or improvement of land, or for the acquisition or improvement of property to be used in connection with the research or experimentation and of a character which is subject to the allowance under § 167 (relating to allowance of depreciation, etc.) or § 611 (relating to allowance for depletion); but for purposes of § 174, allowances under § 167 and allowances under § 611 are considered as expenditures.

(4) Section 174(c)(2) provides that the required § 174 method does not apply to any expenditure paid or incurred for the purpose of ascertaining the existence, location, extent, or quality of any deposit of ore or other mineral (including oil and gas).

(5) Section 174(c)(3) provides that for purposes of § 174, any amount paid or

² The term “capital account” in § 174(a)(2) does not mean the capital account described in § 1.174-1. The term means a separate specified research or experimental capital account.

incurred in connection with the development of any software is treated as a research or experimental expenditure accounted for under the required § 174 method.

(6) Under § 174(d), if any property with respect to which specified research or experimental expenditures are paid or incurred is disposed, retired, or abandoned during the period which such expenditures are allowed as an amortization deduction under the required § 174 method, no deduction is allowed with respect to such expenditures on account of such disposition, retirement, or abandonment and such amortization deduction will continue with respect to such expenditures.

(7) Section 13206(b) of the TCJA provides that the amendments made by § 13206(a) of the TCJA to former § 174 “shall be treated as a change in method of accounting for purposes of section 481” and that “(1) such change shall be treated as initiated by the taxpayer, (2) such change shall be treated as made with the consent of the Secretary, and (3) such change shall be applied only on a cut-off basis for any research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021, and no adjustments under section 481(a) shall be made.”

(8) Section 13206(e) of the TCJA provides that the amendments made by § 13206(a) of the TCJA to former § 174 apply to research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021.

.03 Section 446(e).

(1) Except as otherwise expressly provided in the Code and the regulations thereunder, §§ 446(e) and 1.446-1(e)(2) require a taxpayer to secure the consent of the Commissioner before changing a method of accounting for Federal income tax purposes. Section 1.446-1(e)(3)(i) states, in part, that except as otherwise provided

under the authority of § 1.446-1(e)(3)(ii), to secure the Commissioner's consent to a taxpayer's change in method of accounting the taxpayer generally must file an application on Form 3115, *Application for Change in Accounting Method*, with the Commissioner during the taxable year in which the taxpayer desires to make the change in method of accounting. Section 1.446-1(e)(3)(ii) authorizes the Commissioner to prescribe administrative procedures under which taxpayers will be permitted to change their method of accounting. The administrative procedures will prescribe those terms and conditions necessary to obtain the Commissioner's consent to effect the change and to prevent amounts from being duplicated or omitted.

(2) Rev. Proc. 2015-13, 2015-5 I.R.B. 419, as clarified and modified by Rev. Proc. 2015-33, 2015-24 I.R.B. 1067, and as modified by Rev. Proc. 2017-59, 2017-48 I.R.B. 543, and Rev. Proc. 2021-34, 2021-35 I.R.B. 337, and as updated by Rev. Proc. 2021-26, 2021-22 I.R.B. 1163, sets forth the general procedures by which a taxpayer may obtain the automatic consent of the Commissioner to change a method of accounting described in the *List of Automatic Changes*. Rev. Proc. 2022-14 contains the current *List of Automatic Changes*.

(3) A change in a taxpayer's treatment of specified research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021, to comply with § 174 is a change in method of accounting to which §§ 446(e) and 481, and the corresponding regulations, apply. A taxpayer changing the treatment of specified research or experimental expenditures paid or incurred to the method of accounting that complies with § 174 must use the accounting method change procedures in Rev. Proc. 2015-13, or its successor. Section 3 of this revenue procedure modifies Rev. Proc.

2022-14 to allow taxpayers to obtain automatic consent to change their method of accounting to comply with § 174 for taxable years beginning after December 31, 2021.

(4) As discussed in section 2.02(7) of this revenue procedure, § 13206(b) of the TCJA provides that the amendments made by § 13206(a) of the TCJA to former § 174 are treated as a change in method of accounting for purposes of § 481 that is initiated by the taxpayer and made with the consent of the Commissioner, and that “such change shall be applied only on a cut-off basis for any research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021, and no adjustments under section 481(a) shall be made.” Pursuant to section 2.07 of Rev. Proc. 2015-13, when a change in method of accounting is made without a § 481(a) adjustment (for example, on a cut-off basis), in general, only the items arising on or after the beginning of the year of change, or other operative date, are accounted for under the method of accounting for which consent is granted. Any items arising before the year of change, or other operative date, continue to be accounted for under the taxpayer's former method of accounting. When a change in method of accounting is made on a cut-off basis, no amounts are duplicated or omitted, and therefore, a § 481(a) adjustment is not necessary or permitted.

(5) In accordance with § 13206(b) of the TCJA, a change in a taxpayer's method of accounting to the required § 174 method for the first taxable year that the amendments made by § 13206(a) of the TCJA are effective must be made only on a cut-off basis. The required § 174 method applies only to specified research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021. The procedures in section 3 of this revenue procedure provide an automatic change in

method of accounting to the required § 174 method to comply with § 174 by filing a statement with the taxpayer's original Federal income tax return for the first taxable year in which § 174 becomes effective in lieu of a Form 3115. If a change to the required § 174 method to comply with § 174 for some or all of the taxpayer's specified research or experimental expenditures is made for a taxable year subsequent to the taxable year of the taxpayer in which § 174 becomes effective, the change to the required § 174 method to comply with § 174 is made by filing a Form 3115, with a modified § 481(a) adjustment that takes into account only specified research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021.

(6) Additionally, section 3 of this revenue procedure provides a transition rule for taxpayers who filed a Federal tax return on or before this revenue procedure is published in the Internal Revenue Bulletin for a taxable year beginning after December 31, 2021. The transition rule provides that such taxpayer is deemed to have complied with the § 446 method change procedures and section 7.02 of Rev. Proc. 2022-14, as modified by section 3 of this revenue procedure, if the taxpayer properly reported the amount of specified research or experimental expenditures on Part VI of Form 4562, *Depreciation and Amortization*, filed with the Federal tax return, and properly capitalized and amortized such specified research or experimental expenditures in accordance with the required § 174 method.

(7) A taxpayer that changes its method of accounting for specified research or experimental expenditures under section 7.02 of Rev. Proc. 2022-14, as modified by section 3 of this revenue procedure, will receive limited audit protection under section 8.01 of Rev. Proc. 2015-13. Specifically, audit protection will not apply for expenditures

paid or incurred in taxable years beginning before January 1, 2022. Additionally, notwithstanding the audit protection rules under section 8.01 of Rev. Proc. 2015-13, the IRS may change the characterization or classification of expenditures as specified research or experimental expenditures as defined in § 174(b) in order to apply § 174 as well as the change under section 7.02 of Rev. Proc. 2022-14, as modified by section 3 of this revenue procedure, to the proper amount of expenditures paid or incurred in each taxable year beginning after December 31, 2021.

SECTION 3. AUTOMATIC METHOD CHANGE TO REQUIRED § 174 METHOD

.01 Modification of Section 7 of Rev. Proc. 2022-14. Section 7 of Rev. Proc. 2022-14 is modified to add new section 7.02 to read as follows.

.02 Specified Research or Experimental Expenditures.

(1) Description of change.

(a) This change applies to a taxpayer that changes its method of accounting for specified research or experimental expenditures (as defined under § 174(b)) to the required § 174 method (as defined in section 7.02(1)(b) of this revenue procedure) to comply with § 174. Unless otherwise stated, references to “§ 174” in this section 7.02 refer to § 174 as amended by § 13206(a) of the TCJA. Section 13206(e) of the TCJA provides that the amendments made by § 13206 of the TCJA apply to amounts paid or incurred in taxable years beginning after December 31, 2021.

(b) Section 174(a)(1) provides that in the case of a taxpayer’s specified research or experimental expenditures for any taxable year, except as provided in § 174(a)(2), no deduction is allowed for such expenditures. Section 174(a)(2) provides that the taxpayer must charge such expenditures to capital account and is allowed an

amortization deduction of such expenditures ratably over the 5-year period (15-year period in the case of any specified research or experimental expenditures which are attributable to foreign research within the meaning of § 41(d)(4)(f) of the Code) beginning with the midpoint of the taxable year in which such expenditures are paid or incurred. The method of accounting described in this section 7.02(1)(b) is referred to as the “required § 174 method” in this section 7.02.

(2) Applicability. This change to the required § 174 method applies to specified research or experimental expenditures (as defined in § 174(b)) paid or incurred in taxable years beginning after December 31, 2021.

(3) Inapplicability. This change does not apply to:

(a) a change in the treatment of acquired, leased, or licensed computer software under Rev. Proc. 2000-50, 2000-52 I.R.B. 601, as modified by Rev. Proc. 2007-16, 2007-1 C.B. 358 (see section 9.01 of this revenue procedure); or

(b) a change in the treatment of research or experimental expenditures under former § 174, or software development expenditures, paid or incurred in taxable years beginning before January 1, 2022 (see sections 7.01 and 9.01 of this revenue procedure).

(4) Manner of making change.

(a) First taxable year beginning after December 31, 2021.

(i) Cut-off basis. The change under section 7.02 of this revenue procedure for specified research or experimental expenditures paid or incurred in the first taxable year beginning after December 31, 2021, is implemented on a cut-off basis.

(ii) Statement in lieu of a Form 3115 for first taxable year beginning after

December 31, 2021. Except as otherwise provided in section 7.02(5) of this revenue procedure, the requirement of § 1.446-1(e)(3)(i) to file a Form 3115, *Application for Change in Accounting Method*, is waived and a statement in lieu of a Form 3115 is authorized for the change in method of accounting under section 7.02 of this revenue procedure for which the year of change is the first taxable year beginning after December 31, 2021. Notwithstanding the definition of Form 3115 in section 3.07 of Rev. Proc. 2015-13, 2015-5 I.R.B. 419, the statement in lieu of a Form 3115 that is permitted under this section 7.02(4)(a)(ii) is considered a Form 3115 for purposes of the automatic consent procedures of Rev. Proc. 2015-13. The requirement to file the duplicate copy, under section 6.03(1)(a) of Rev. Proc. 2015-13, is waived. The statement must include the following information for each applicant:

(A) the name and employer identification number or social security number, as applicable, of the applicant that has paid or incurred specified research or experimental expenditures after December 31, 2021;

(B) the beginning and ending dates of the first taxable year in which the change to the required § 174 method takes effect for the applicant (year of change);

(C) the designated automatic accounting method change number for this change (see section 7.02(8) of this revenue procedure);

(D) a description of the type of expenditures included as specified research or experimental expenditures;

(E) the amount of specified research or experimental expenditures paid or incurred by the applicant during the year of change; and

(F) a declaration that the applicant is changing the method of accounting for

specified research or experimental expenditures to capitalize such expenditures to a specified research or experimental capital account, and amortize such amount over either a 5-year period for domestic research or 15-year period for foreign research (as applicable) beginning with the mid-point of the taxable year in which such expenditures are paid or incurred in accordance with the method permitted under § 174 for the year of change. Also, the declaration must state that the applicant is making the change on a cut-off basis.

(b) Year of change later than the first taxable year beginning after December 31, 2021.

(i) Modified § 481(a) adjustment. The change under section 7.02 of this revenue procedure for a year of change later than the first taxable year beginning after December 31, 2021, is made with a modified § 481(a) adjustment, and should take into account only specified research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021.

(ii) Form 3115. In completing a Form 3115, *Application for Change in Accounting Method*, to make the change in method of accounting under section 7.02 of this revenue procedure with respect to any year of change later than the first taxable year beginning after December 31, 2021, a taxpayer must include on an attachment to Form 3115:

(A) a description of the type of expenditures included as specified research or experimental expenditures;

(B) the taxable year(s) in which the specified research or experimental expenditures subject to the change were paid or incurred by the applicant; and

(C) a declaration that the applicant is changing its method of accounting for specified research or experimental expenditures to capitalize such expenditures to a specified research or experimental capital account, and amortize such amount over either a 5-year period for domestic research or 15-year period for foreign research (as applicable) beginning with the mid-point of the taxable year in which such expenditures are paid or incurred in accordance with the method permitted under § 174 for the year of change. Also, the declaration must state that the applicant is making the change with a modified § 481(a) adjustment that takes into account only specified research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021.

(5) Transition rule. A taxpayer who filed a Federal tax return on or before January 9, 2023, for a taxable year beginning after December 31, 2021, is deemed to have complied with the § 446 method change procedures and section 7.02 of this revenue procedure to change its method of accounting for specified research or experimental expenditures paid or incurred in the first taxable year beginning after December 31, 2021, to the required § 174 method to comply with § 174 if the taxpayer:

(a) reported the amount of specified research or experimental expenditures paid or incurred for such taxable year on Part VI of Form 4562, *Depreciation and Amortization*, filed with the Federal tax return, and

(b) properly capitalized and amortized such specified research or experimental expenditures in accordance with the required § 174 method for such taxable year.

(6) Certain eligibility rule temporarily inapplicable. The eligibility rule in section 5.01(1)(f) of Rev. Proc. 2015-13, 2015-5 I.R.B. 419, does not apply to changes to the

required § 174 method for the taxpayer's first taxable year beginning after December 31, 2021.

(7) No audit protection for expenditures paid or incurred in taxable years prior to the first taxable year in which § 174 becomes effective. A taxpayer does not receive audit protection under section 8.01 of Rev. Proc. 2015-13 for the change under section 7.02 of this revenue procedure with respect to expenditures paid or incurred in taxable years beginning on or before December 31, 2021. See section 8.02(2) of Rev. Proc. 2015-13.

(8) Designated automatic accounting method change number. The designated automatic accounting method change number for a change under section 7.02 of this revenue procedure is "265."

(9) No inference relating to expenditures paid or incurred in taxable years prior to the first taxable year in which § 174 becomes effective. No inference may be drawn from section 7.02 of this revenue procedure regarding the treatment of research or experimental expenditures paid or incurred in, and changes in methods of accounting for, taxable years in which former § 174 was in effect, including issues relating to the application of §§ 1.174-1, 1.174-3, and 1.174-4 of the Income Tax Regulations for taxable years in which former § 174 was in effect.

(10) Contact information. For further information regarding a change under this section, contact Martha M. Garcia at (202) 317-6853 (not a toll-free number).

SECTION 4. EFFECT ON OTHER DOCUMENTS

This revenue procedure modifies section 7 of Rev. Proc. 2022-14.

SECTION 5. EFFECTIVE DATE

This revenue procedure is effective for specified research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2021, in which § 174 is in effect.

SECTION 6. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget under OMB control numbers 1545-0074 for individual filers and 1545-0123 for business filers, in accordance with the Paperwork Reduction Act (44 U.S.C. 3507(d)). 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 OMB control number. The collection of information in this revenue procedure is in section 3, which adds sections 7.02(4)(a)(ii) and 7.02(4)(b)(ii) to Rev. Proc. 2022-14. This information is necessary and will be used to determine whether the taxpayer properly changed to a permitted method of accounting. The collections of information are required for the taxpayer to obtain consent to change its method of accounting.

SECTION 7. DRAFTING INFORMATION

The principal authors of this revenue procedure are Martha M. Garcia and John M. Deininger of the Office of Associate Chief Counsel (Passthroughs & Special Industries). For further information regarding this revenue procedure contact Martha M. Garcia or John M. Deininger at (202) 317-6853 (not a toll-free call).