

## IRS Releases An Advanced Version Of Rev. Rul. 2023-8, Replacing Rev. Rul. 58-74

The IRS released an advanced version of Rev. Rul. 2023-8, which obsoletes Rev. Rul. 58-74 effective as of July 31, 2023, due to insufficient facts in the ruling.

Before the Tax Cuts and Jobs Act (TCJA), section 174(a) permitted a taxpayer to currently deduct R&E expenditures (the “expense method”). However, if the expense method was adopted, it had to be used for all qualifying expenditures in the tax year and subsequent years unless the IRS Commissioner consented to a different method for all or part of the expenditures under former section 174(a)(3).

The TCJA amended section 174 to provide that R&E costs incurred in tax years beginning after December 31, 2021, must be capitalized, and amortized over five years if the research is performed in the United States and over 15 years if performed outside of the United States.

Rev. Rul. 58-74 provides that if a taxpayer adopted the expense method but failed to deduct expenses relating to the cost of obtaining a patent or other items of R&E expenditures for prior tax years, they must file a claim for refund or amended return to deduct additional R&E expenditures in the year or years when the expenditures were paid or accrued. Additionally, the additional R&E expenditures cannot be treated as deferred and amortized under former section 174(b) or chargeable to the capital account and subsequently amortized or written off upon abandonment of the project or projects because the Commissioner’s consent to change a method of accounting was not obtained. Therefore, the deduction for the additional R&E expenditures could be lost if the period of limitations on claims for credit or refund under section 6511 has expired and amended returns could not be timely filed.

The Treasury Department and the IRS are obsoleting Rev. Rul. 58-74 not because of the change in law under section 174, however, but because there are insufficient facts in the ruling to properly analyze whether the taxpayer’s failure to deduct certain R&E expenditures constituted accounting method or an error. Some of the reasons for obsoleting Rev. Rul. 58-74 are as follows:

- Rev. Rul. 58-74 does not explain whether the taxpayer consistently treated the costs of obtaining a patent in determining its taxable income.
- Rev. Rul. 58-74 also fails to describe the cause and extent of the deviation in treating certain R&E expenditures that were not deducted.
- If the facts demonstrate that a taxpayer has a changed accounting method, then filing an amended return, refund claim, or administrative adjustment request (AAR) under section 6227 in reliance upon Rev. Rul. 58-74 would conflict with the statutory requirement that a taxpayer must secure the consent of the Commissioner to change a method of accounting.
- Thus, Rev. Rul. 58-74 is no longer determinative.

The taxpayer may still file a claim for refund, amended return, or AAR in reliance on Rev. Rul. 58-74 before that date, because Rev. Rul. 2023-8 obsoletes Rev. Rul. 58-74 as of July 31, 2023.