

MEMO# 15474

December 19, 2002

IRS ISSUES PROPOSED REGULATIONS REGARDING CAPITALIZATION OF INTANGIBLE ASSETS

[15474] December 19, 2002 TO: TAX COMMITTEE No. 41-02 RE: IRS ISSUES PROPOSED REGULATIONS REGARDING CAPITALIZATION OF INTANGIBLE ASSETS The Internal Revenue Service (the "Service") has issued proposed regulations¹ regarding the deductibility or capitalization of amounts paid to acquire, create, or enhance intangible assets. The proposed regulations generally follow the approach outlined in the Advance Notice of Proposed Rulemaking (the "Advance Notice") issued by the Service earlier this year² that described (1) specific categories of expenditures incurred in acquiring, creating or enhancing intangible assets or benefits that taxpayers are required to capitalize and (2) certain types of transaction costs otherwise capitalizable that nevertheless would be deductible. The proposed regulations confirm that certain enumerated internal transaction costs including "compensation [including bonuses and commissions] paid to employees, overhead, and de minimis costs" are not required to be capitalized, as they are not treated as amounts that facilitate a transaction. Thus, as urged by the Institute, a fund sponsor's internal costs of creating new funds are deductible.³ The proposed regulations, however, do not adopt the Institute's suggestion that independent contractors who function as employees be treated as employees, where the independent contractors facilitate a transaction otherwise subject to capitalization.⁴ As requested by the Institute, the preamble to the proposed regulations also confirms the continuing vitality of Revenue Ruling 94-705 - which concludes that open-end investment companies may deduct stock issuance costs (other than those related to the initial stock offering). 1 The proposed regulations are available at <http://www.treas.gov/press/releases/reports/cap.pdf> and are attached to the electronic version of this memorandum. 2 See, Institute Memorandum to Tax Members No. 5-02, dated January 25, 2002. 3 See, Institute Memorandum to Tax Members No. 15-02, dated March 25, 2002. 4 The proposed regulations specify that only compensation paid to employees as defined in Code section 3401(c) satisfies the "simplifying convention" adopted with respect to internal costs. 5 1994-2 C.B. 17. 2 ACTION REQUESTED Comments on the proposed regulations are due by March 19, 2003. Please contact the undersigned (202/326-5821 or cbarre@ici.org) by February 19 with any comments that you would like the Institute to submit on the proposed regulations. Catherine Barré Assistant Counsel Attachment (in .pdf format)

should not be considered a substitute for, legal advice.