

October 6, 2003

Submitted to www.irs.gov/regs. and hand delivered

The Honorable Mark Everson
Commissioner
Internal Revenue Service
Attn: CC:PA:RU (REG-138495-02)
Courier's Desk
1111 Constitution Avenue, N.W.
Washington, DC 20044

Re: Notice of Proposed Rulemaking by Cross Reference to Temporary Regulations; Depreciation of Vans and Light Trucks, REG-138495-02, 68 Fed. Reg. 40224 (July 7, 2003).

Dear Commissioner Everson:

The Office of Advocacy (Advocacy) of the U.S. Small Business Administration (SBA) submits these comments for the record in the above-referenced rulemaking. In the event a hearing on this issue is scheduled, we request the opportunity to appear and ask that this letter also serve as the outline of our testimony.

On July 7, 2003, the Internal Revenue Service (IRS) issued a notice of proposed rulemaking by cross reference to temporary regulations that modify existing regulations relating to limitations on the depreciation allowance for passenger automobiles by excluding certain vans and light duty trucks.¹ This proposed rule was long sought by the small business community. It will have a significant beneficial impact on a substantial number of small businesses. Advocacy commends the IRS for its outreach to small entities to solicit their comments and make its intentions known. Based on input from affected small entities, Advocacy recommends the IRS consider expanding the regulations to cover more light trucks and vans used by taxpayers in business and trade. Advocacy believes an objective standard can be based on use of the vehicle rather than by limiting the exception to specially modified vehicles. Advocacy urges the IRS to perform a regulatory flexibility analysis, as required by the Regulatory Flexibility Act, to obtain the information necessary to assess regulatory alternatives that meet statutory objectives and exclude vans and light duty trucks used in business and trade by small businesses.

Advocacy Background

The Office of Advocacy was established pursuant to Pub. L. 94-305 to represent the views of small business before Federal agencies and Congress. Advocacy is an independent office within the U.S. Small Business Administration, so the views expressed by Advocacy do not necessarily

¹ 68 Fed. Reg. 40224 (July 7, 2003).

reflect the views of the SBA or the Administration. Advocacy is also responsible for monitoring agency compliance with the Regulatory Flexibility Act (RFA), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).² The RFA requires Federal agencies, such as the IRS, to analyze the impact on small entities and consider alternatives to avoid overly burdensome regulation of small entities.³

On August 13, 2002, President George W. Bush signed Executive Order 13272, requiring Federal agencies to implement policies protecting small businesses when writing new rules and regulations.⁴ Executive Order 13272 instructs Advocacy to provide comment on draft rules to the agency that has proposed a rule, as well as to the Office of Information and Regulatory Affairs (OIRA) of the Office of Management and Budget.⁵ Executive Order 13272 also requires agencies to give every appropriate consideration to any comments provided by Advocacy. Under the Executive Order, the agency must include, in any explanation or discussion accompanying publication in the *Federal Register* of a final rule, the agency's response to any written comments submitted by Advocacy on the proposed rule, unless the agency certifies that the public interest is not served by doing so.⁶

Applicability of the Regulatory Flexibility Act

The RFA applies “whenever an agency is required by §553 of [the Administrative Procedure Act (APA)], or any other law, to publish general notice of proposed rulemaking”⁷ While the APA exempts certain IRS interpretative rules from notice and comment rulemaking, notice and comment is required for substantive, legislative rules. Advocacy believes this rulemaking involves a legislative rule.

Internal Revenue Code section 280F imposes a limitation on the amount of depreciation that can be claimed on passenger automobiles. Recognizing the special character of vans and light trucks, Congress provided an exemption for vans and light trucks, leaving a gap in the statutory scheme, but provided specific authority for the IRS to fill the gap by defining through regulation which vans and light trucks would be exempt.⁸ Advocacy believes this is an inherently legislative rulemaking that requires notice and comment rulemaking under the APA and therefore compliance with the RFA.⁹

An Administrable Objective Standard

To fill the gap left in section 280F, the IRS' temporary and proposed rules exclude from the passenger vehicle depreciation requirements those vans and light trucks that are “specially

² Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164 (1981) (codified as amended at 5 U.S.C. §§ 601-612).

³ Pub. L. No. 96-354, 94 Stat. 1164 (1981) (codified as amended at 5 U.S.C. §§ 601-612).

⁴ Exec. Order No. 13,272 § 1, 67 *Fed. Reg.* 53,461 (Aug. 13, 2002) (“E.O. 13272”).

⁵ E.O. 13272, at § 2(c), 67 *Fed. Reg.* at 53,461.

⁶ *Id.* at § 3(c), 67 *Fed. Reg.* at 53,461.

⁷ 5 U.S.C. §603(a).

⁸ 26 U.S.C. 280 F(d)(5)(B)(iii) provides that: “the term ‘passenger automobile’ shall not include... (iii) under regulations, any truck or van.”

⁹ *Bankers Life and Cas. Co. v. United States*, 142 F.3rd 973, 978 (7th Cir.), *cert. denied*, 525 U.S. 961 (1998).

modified with the result that it is not likely to be used more than a de minimis amount for personal purposes.”¹⁰ This approach has the advantage of being simple and rather straightforward in its application. However, it has the disadvantage of unnecessarily excluding many vans and light trucks required in trade and business that do not require alteration of the vehicle’s structure. Advocacy encourages the IRS to engage the small business community in developing an alternate approach that recognizes the vehicles used for valid business purposes without the need for alteration or modification and signage. The analysis required under the RFA includes the identification of affected parties, analysis of impacts and consideration of alternatives – all of which could assist the IRS in identifying an alternate objective standard based on use rather than modification of the vehicle.

Significant Economic Impact on a Substantial Number of Small Businesses

Under the RFA, if the rule may have a significant economic impact on a substantial number of small entities, an initial regulatory flexibility analysis must be performed.¹¹ This proposed rule is having a tremendous impact on tens of thousands of small businesses. Advocacy solicited input on the rule’s impact from associations and representatives of small businesses that use vans and light trucks. Businesses that significantly modify their vans and trucks by removing seats, installing racks or other specialized equipment, and painting advertising on the sides of their trucks expressed satisfaction with the proposed rule. Because their vehicles meet the exclusion in the IRS’ temporary and proposed rules, they are already reaping the benefits of their vehicles being excluded from the depreciation limitations. Other small businesses, such as those overseeing fleet services, in traveling sales, service and repair, and funeral homes or farm-related businesses, expressed concern that their vehicles, though used exclusively in trade or businesses, will not qualify for the exclusion because the vehicles are not modified or manufactured for specific business purpose. Consequently, the taxpayer must comply with the lower depreciation caps for these business vans and light duty trucks.¹²

The IRS chose to define which vans and light trucks are excluded from the depreciation cap by requiring that the vehicle must be specially manufactured or modified so that it is not likely to be used more than a de minimis amount for personal purposes.¹³ Advocacy believes there are other appropriate methods that can provide objective standards for defining light duty trucks and vans used in trade or business and assure de minimis amount of personal use. Congress specifically included trucks and vans as vehicles that could be excluded by regulation. It is fair to conclude

¹⁰ 26 C.F.R. § 1.274-5(T)(k)(7).

¹¹ In lieu of an initial regulatory flexibility analysis as required under § 603 of the RFA, an agency head may certify that a rule will not have a significant economic impact on a substantial number of small entities under § 605(b) of the RFA. A certification statement must be accompanied by a factual basis in support of the certification. Advocacy recommends that agencies perform a preliminary or threshold analysis to determine if certification is appropriate. For more information on performing a threshold analysis or initial regulatory flexibility analysis, please see *A Guide for Government Agencies: How to Comply with the Regulatory Flexibility Analysis*, available on Advocacy’s website at <http://www.sba.gov/advo/laws/rfaguide.pdf>.

¹² On October 2, 2003, the IRS released Revenue Procedure RP-2003-75, which provides a slight increase in the depreciation cap (based on inflation rates) for non-modified light trucks and vans. While very helpful, even when combined with higher 50% “bonus depreciation” provisions of the Jobs and Growth Reconciliation Act of 2003 the maximum that can be written off is \$23,610 over 5 years. The cost of most light trucks and vans will exceed the allowable depreciation.

¹³ See the Preamble of the Temporary Regulations at 68 Fed. Reg. 40129.

that they recognized the special, working character of these vehicles and sought, with the help of the IRS, to separate light trucks and vans required in business or trade from passenger automobiles used similarly. The important consideration for vans and light trucks is, we believe, how the vehicle is used. If the business owner can substantiate a need to have a light truck or van for a valid business or trade purpose and it is used as such, Advocacy believes Congress intended to exclude such vehicles from the limits it placed on depreciation for passenger vehicles. Advocacy believes the IRS proposal is more restrictive than necessary and that an alternate objective standard should be developed.

Conclusion

This proposed rule confers a substantial benefit on certain small businesses - specifically owners of substantially modified light trucks and vans weighing less than 6,000 pounds. Through its compliance with the RFA, the IRS can investigate approaches that would confer a broader exclusion and more accurately reflect the use and value to the business of the vehicles. With the benefit of small entity outreach, the IRS can identify alternatives that meet the statutory objective without imposing undue burdens on small entities.

Advocacy urges the IRS to give full consideration to expanding the scope of the regulation to include light trucks and vans that are not modified or manufactured for a specialized business or trade purpose for which an appropriate business or trade requirement can be substantiated. Our office would be happy to help the IRS confer with small business groups about ways to structure the regulation to be as useful as possible for small entities.

Thank you for your consideration in this matter. For additional information or to discuss Advocacy's comments, please do not hesitate to contact me or Russell Orban, (202) 205-6533 or russell.orban@sba.gov, of my staff.

Sincerely,

Thomas M. Sullivan
Chief Counsel for Advocacy

Russell Orban
Assistant Chief Counsel for Tax

Cc: Dr. John D. Graham, Administrator, Office of Information and Regulatory Affairs