EXHIBIT 9 – 1

GAAP AND POLICIES & PROCEDURES

IRS RULES

AUDIT FINDING #9

GAAP Handbook of Policies and Procedures

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ENVIRONMENTAL

As per Emerging Issues Task Force Consensus Summary Number 90–8 (*Capitalization of Costs to Treat Environmental Contamination*), the costs to prevent, contain, or remove environmental contamination should be expensed. **Exception:** These costs can be deferred to the fixed asset in the following cases:

- The costs increase the asset's life or capacity or improve its efficiency or safety.
- The costs are incurred to prepare the property for sale.

According to Emerging Issues Task Force Consensus Summary Number 89–13 (*Accounting for the Cost of Asbestos Removal*), the cost to treat property bought having an asbestos problem should be deferred to the asset. Disclosure should be made of the asbestos problems amd related costs to correct.

DEPRECIATION

If a fixed asset is bought during the year, there will be fractional year depreciation requiring proration.

Land and Land Improvements

The cost of land includes closing costs (e.g., attorney fees, recording fees), costs to get land in condition for intended use (e.g., grading, draining, filling), assumption of any liens or encumbrances on the property, and costs to remove an old structure to build on the property. For example, if an old building is torn down to make way for the construction of a new building, the demolition costs are charged to land.

Land held for investment, speculation, or a future plant site should be classified under investments rather than fixed assets.

Land held for resale by a real estate company is considered inventory.

Land improvements such as fences, driveways, sidewalks, and parking lots are deferred and depreciated over their useful lives.

Repairs

Ordinary repairs such as a tune-up for a delivery truck are expensed because they only benefit less than one year.

Extraordinary repairs are deferred to the fixed asset because they benefit more than one year. An example is a new motor for a salesperson's automobile. Extraordinary repairs either increase the asset's life or make the asset more useful. Capital expenditures enhance the quality or quantity of services to be obtained from the asset.

Proposed regulation by IRS 8/21/06 reg# 168745-03

In contrast to the cases discussed above, both the courts and the IRS have permitted a current deduction for some government mandated expenditures. For example, in *Midland Empire Packing Co. v. Commissioner*, 14 T.C. 635 (1950), acq. (1950-2 C.B. 3), the court allowed the taxpayer to deduct the costs of applying a concrete liner to its basement walls to satisfy Federal meat inspectors. Similarly, the IRS has permitted taxpayers to treat as otherwise deductible repairs amounts paid to remediate certain environmental contamination and to replace certain waste storage tanks to comply with applicable state and Federal regulations. See Rev. Rul. 94-38 (1994-1 C.B. 35); Rev. Rul. 98-25 (1998-1 C.B. 998). The IRS specifically recognized in Rev. Rul. 2001-4 (2001-1 C.B. 295) that the requirement of a regulatory authority to make certain repairs or to perform certain maintenance on an asset to continue operating the asset does not mean that the work performed must be capitalized. Thus, the proposed regulations reiterate that statement in Rev. Rul. 2001-4 and provide that a legal compulsion to repair or maintain tangible property is not a relevant factor in the repair versus improvement analysis. The IRS and Treasury Department further believe that a new government requirement for existing property that mandates certain expenditures with respect to the property does not create an inherent defect in the property.

In response to several comments, the proposed regulations provide that if a taxpayer needs to replace part of a unit of property that cannot practicably be replaced with the same type of part, the replacement of the part with an improved but comparable part does not, by itself, result in an improvement to the unit of property. This rule is intended to apply in cases where the same replacement part is no longer available, generally because of technological advancements or product enhancements. This rule, however, is not intended to apply if, instead of replacing an obsolete part with the most similar comparable part available, the taxpayer replaces the part with one of a better quality than what would have sufficed.

The proposed regulations do not prescribe a plan of rehabilitation doctrine as traditionally described in the case law. That judicially-created doctrine provides that a taxpayer must capitalize otherwise deductible repair costs if they are incurred as part of a general plan of rehabilitation to the property. See, *Norwest Corp. v. Commissioner*, 108 T.C. 265 (1997); *Moss v. Commissioner*, 831 F.2d 833 (9th Cir. 1987); *United States v. Wehrli*, 400 F.2d 686 (10th Cir. 1968). Specifically, if an expenditure is made as part of a general plan of rehabilitation, modernization, and improvement of the property, the expenditure must be capitalized, even though, standing alone, the item may be classified as one of repair or maintenance. *Wehrli*, 400 F.2d at 689. Whether a general plan of rehabilitation exists, and whether a particular repair or maintenance item is part of it, are questions of fact to be determined based upon all the surrounding facts and circumstances, including, but not limited to, the purpose, nature, extent, and value of the work done. *Id.* at 690.

The issue of whether an amount paid must be capitalized under the plan of rehabilitation doctrine has been the subject of much litigation, with varying results. For example, some cases have limited application of the plan of rehabilitation doctrine to buildings that are not suitable for their intended use in the taxpayer's trade or business. See *Schroeder v. Commissioner*, T.C. Memo 1996-336; *Koanis v. Commissioner*, T.C. Memo 1978- 184, aff'd mem., 639 F.2d 788 (9th Cir. 1981); *Keller Street Dev. Co. v. Commissioner*, 37 T.C. 559 (1961); acq., 1962-2 C.B. 5, aff'd in part, rev'd in part on other grounds, 323 F.2d 166 (9th Cir. 1963). Other courts, as well as the

IRS, have viewed the plan of rehabilitation doctrine more broadly, emphasizing the planned aspect of the work done by the taxpayer, rather than the condition of the property. See *Mountain Fuel Supply Co. v. United States*, 449 F.2d 816 (10th Cir. 1971); *Wolfsen Land & Cattle Co. v. Commissioner*, 72 T.C. 1 (1979); Rev. Rul. 88-57 (1988-2 C.B. 36).