

WHEN IS YOUR WEB SITE DEDUCTIBLE?

Costs associated with site design and construction may be allowable, but since the IRS has never issued formal guidance, it's not so simple.

Q I'm wondering whether I can deduct the cost of designing and constructing a Web site for my business. The total cost will be \$27,000, which we've paid to an outside consultant who took on the job. Can I amortize the expense over 15 years as an "intangible" under tax section 197?

-- K.M., Lynnfield, Mass

A Yours is a tough question, tax experts say. Does Web-site development fall under the "intangible" category of tax section 197 to be amortized over 15 years, or should the expense be deducted immediately as a professional fee? Or does another way exist to account for the expense? While there has been massive growth in Web-site development costs over the past few years, the IRS hasn't issued formal guidance on the proper tax treatment of these expenses.

Without explicit guidelines on record at the IRS, your best bet is to get professional advice from your accountant or tax preparer specifically for your situation. Three experts we consulted acknowledged that the problem is complex, but all agreed that it's unlikely that section 197 would apply to you.

DIFFERENT APPROACHES

"Since a Web site is continuously being tweaked, changed, and updated, a 15-year life seems out of line," says Donald Lucove, a CPA with Lucove, Say & Co. in Calabasas, Calif. "These expenditures would likely fall into the classification of software and be considered a three-year depreciable item."

Because you had your Web site designed by an independent contractor, your business can choose among alternative tax treatments, says Bradford Hall, managing director of Hall & Co. CPAs in Irvine, Calif. You could amortize the cost under the three-year rule, he says, or deduct the cost in total as an advertising expense.

SPREADING IT OUT

Be cautious if you're interested in adopting the latter approach, however, Hall advises. In a January, 2002, tax-court case, a taxpayer was successful in deducting the entire cost of developing his Web site as advertising expense. "The taxpayer spent funds to develop an Internet Web site to promote his architectural computer-aided design drafting services, even though the Web site was never completed," Hall

says. "Had the Web site been completed, the IRS may have been successful in asserting that the costs associated with the overall Web site structure, functionality, and appearance must be capitalized and amortized over a longer useful life."

On a separate note, don't forget to issue a tax form 1099 to the consultant who did the Web-site design and development, if he or she operates as a noncorporate entity.

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