



OFFICE OF
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
August 30, 1999

Number: **199950004**
Release Date: 12/17/1999
CC:DOM:FS:P&SI

UILC: 168.18-00; 168.20-00

INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

DISTRICT COUNSEL

ATTN:

FROM: DEBORAH A. BUTLER
ASSISTANT CHIEF COUNSEL (FIELD SERVICE)
CC:DOM:FS

SUBJECT: DEPRECIATION / RECOVERY PERIOD

This Field Service Advice responds to your memorandum dated May 24, 1999. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND:

T =
Date =
State =
River =
Canal =
County =
Facility =
Building Code =
Case 1 =

Case 2 =

Case 3 =

Case 4 =

Case 5 =

ISSUE(S):

1. How strong is the Service's contention that, for depreciation purposes, a Facility built on a barge is nonresidential real property with an appropriate recovery period of 39 years?
2. What, if any, additional development should be undertaken to develop this case?

CONCLUSION:

1. Further factual development is needed before we can comment on the strength of the Service's contention.
2. We agree that the factors mentioned in your incoming memorandum are relevant. In addition, we suggest, as detailed below, that certain factual areas be explored as well.

FACTS:

T owns and operates a licensed Facility which was constructed on a barge and placed in service on Date. The Facility was partially constructed at a shipyard and was towed by a tugboat to its current site. Three stories were erected on the barge. The Facility is located in the Canal. The Facility is in a man-made cofferdam with a special anchoring system which separates the Facility from River. There is no navigable waterway from the cofferdam to River.

A platform is pinned to the Facility and extends to the land to allow access to the Facility. The Facility is also affixed to the land through an anchoring system. All support services such as kitchens, mechanical systems, administrative and dining areas are located in the buildings on the adjacent land. Water, electrical power, and telephone services are provided by local utility companies through supply and return lines attached to the Facility.

A building permit was obtained from County prior to constructing the Facility. The Facility is required to comply with the Building Code. The Facility has fire insurance based on a classification as real property. The Facility has a structural steel frame, walls, and roof, all of which enclose a volume of space and was constructed from commonly used building materials. The blueprints used to construct the Facility are of the type used for buildings rather than boats.

At issue is the recovery period of the Facility. T has treated the Facility as a vessel, barge, tug or similar water transportation equipment with a recovery period of 10 years as an asset in Class 00.28 pursuant to Rev. Proc. 87-56, 1987-2 C.B. 674. It is the Service's contention that the Facility is nonresidential real property with a recovery period of 39 years¹ pursuant to section 168(c), as was in effect for the taxable years at issue. This matter is not docketed and is under consideration by the District Director.

LAW AND ANALYSIS

A "vessel" includes every description of water craft or other artificial contrivance used, or capable of being used, as a means of transportation on water. 1 U.S.C. § 3. There is no more specific definition of a vessel, barge, tug, or similar water transportation equipment in the Internal Revenue Code. We agree that while the cases cited are not controlling, they are informative. See e.g., Case 1; Case 2; Case 3; Case 4; Case 5. As a practical guide consistent with the foregoing cases, we believe that a Facility which was certified by the U.S. Coast Guard for use to transport persons or cargo on water for production of income in furtherance of the taxpayer's business during the taxable year(s) in issue may be included in asset class 00.28. For these purposes, the taxpayer need not be in the business of water transportation and need not have actually carried passengers or cargo during the taxable year(s) in issue. Certification or loss of certification during the Facility's recovery period would be considered a change in use under section 168(i)(5).

From the information provided, we do not know if the Facility was certified during the year(s) in issue as described herein. Although inquiry may end here if the Facility was certified as described herein during the taxable year(s) in issue, we continue the analysis necessary to determine the appropriate recovery period.

Based upon the facts provided, the activity in which the asset is primarily used is otherwise described in asset class 79.00, because that asset class includes assets used in the provision of entertainment services. Asset class 79.00 specifically

¹Nonresidential real property placed in service after May 12, 1993 has a recovery period of 39 years; Nonresidential real property placed in service after 1986 and before May 13, 1993 has a recovery period of 31.5 years. I.R.C. §168(c).

excludes buildings which house the assets used in entertainment services.

The Internal Revenue Code defines nonresidential real property for depreciation purposes by reference to section 1250 and the regulations thereunder. E.g. I.R.C. § 168(e)(2)(B); Treas. Reg. § 1.167(a)-11(b)(2). Section 168(i)(12) provides that 1250 property has the same meaning as given in section 1250(c). Section 1250 property, is defined as any real property, other than section 1245 property, which is or has been of a character subject to the allowance for depreciation provided in section 167. I.R.C. §1250(c). Section 1245 property is any property of a character subject to the allowance for depreciation under section 167 and is either (a) personal property, (b) other tangible property (not including a building or its structural components) used in connection with a qualified activity or a research or storage facility used with a qualified activity, (c) a single purpose agricultural or horticultural structure, (d) a storage facility used in connection with the distribution of petroleum). I.R.C. §1245(a)(3). The terms “buildings” and “structural components” have the meanings assigned to those terms in Treasury Regulation section 1.48-1(e). Treas. Reg. § 1.1245-3(c)(2). A building is defined in Treasury Regulation section 1.48-1(e)(1) as any structure or edifice enclosing a space within its walls, and usually covered by a roof, the purpose of which is, for example, to provide shelter or housing, or to provide working, office, parking, display, or sales space.

Of further relevance in determining whether a structure is a building are inherent permanency, the appearance, and the function of the structure. See L.L. Bean, Inc. v. Commissioner, T.C. Memo 1997-175. Determining if a structure is inherently permanent requires a consideration of six factors set forth in Whiteco Industries, Inc. v. Commissioner, 65 T.C. 664, 672-73 (1975). Those factors are: (1) the manner in which the property is affixed to the real property; (2) whether the property was designed to be easily removable or to remain in place indefinitely; (3) whether the property has been moved since its initial installation; (4) any circumstances that suggest the expected period of affixation (e.g., a lease that requires removal of the property upon its expiration); (5) the amount of damage that removal of the property will cause, in terms of time and expense.

While additional factual development is needed, there are numerous factors which lend to the conclusion that the Facility is nonresidential real property with a recovery period of 39 years. For instance, a platform is pinned to the Facility and extends to the land. The Facility is also affixed to the land through an anchoring system. Water, electrical power, and telephone services are provided by local utility companies through supply and return lines attached to the Facility. The Facility appears to not be easily removable from its current site. A towing company and engineering firm will need to be hired to relocate the Facility. The move would require disconnecting all utilities and support systems, dredging channels,

provisions for a spoil material receiving area, cofferdam removal, and compliance with all governmental permits and environmental law. In addition, the Facility has not been moved since its installation.

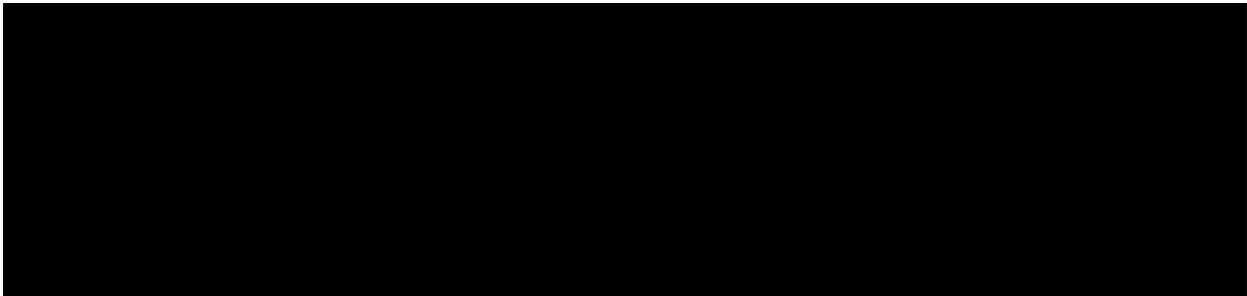
The appearance test, whether the structure looks like a building, generally requires a structure enclosing a space within its walls and covered by a roof. See Treas. Reg. §1.48-1(e)(1); L.L. Bean, Inc., supra. For visual effect only, the Facility is designed to give the appearance of a boat. These physical attributes, however, are not intended to function as a boat. From the inside, the Facility appears to be a building with walls, hallways, and a roof.

The function test focuses on whether the structure provides working space for employees that is more than merely incidental to the primary function of the structure. This requires consideration of both the quantity and quality of the human activity in the structure. See L.L. Bean, Inc., supra. The Facility functions as a structure to house recreation for its patrons. The shelter provided to enable the employees to provide entertainment is merely incidental to this primary function.

We agree that while Rev. Rul. 77-21, 1977-1 C.B. 251, is not directly on point, it is informative to the present inquiry. We also agree with your analysis that the Facility is significantly different from the floating docks found to be personal property in Estate of Shirley Morgan v. Commissioner, 52 T.C. 478 (1969) and Rev. Rul. 75-178, 1975-1 C.B. 9; and the mobile homes which were in Moore v. Commissioner, 58 T.C. 1045 (1972).

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS:

The successful resolution of this case involves intensive factual development because neither section 168, Rev. Proc. 87-56, nor its predecessors, define what assets are considered barges under asset class 00.28. We encourage you to work closely with your experts to further develop this case. We concur in large part with your analysis and factual development in your memorandum. However, additional inquiry is needed before we can comment on the strength of the Service's contention.



2 [REDACTED]

[REDACTED]

As reflected in the analysis section of this memorandum, we disagree with the interpretation of asset class 00.28 in the engineering report wherein it is stated that this asset class requires the asset to be used in the water transportation business or industry. We do not find support for this assertion in Rev. Proc. 87-56 or section 167. Further, section 167(a) provides that there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear of property used in the taxpayer's trade or business or property held for the production of income. Section 167(a) requires that the asset be used in the taxpayer's trade or business without regard to the type of asset and trade.

Once we have determined that the asset is not properly classified in asset class 00.28, we need to determine if the asset is section 1250 property (nonresidential real property) or other property under asset class 79.00.

[REDACTED]

[REDACTED]

2 [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

The state of the law falls between the Tax Court's more recent and favorable decision in L.L. Bean, supra, (where the court found that a storage facility connected at the mezzanine level to adjacent buildings were inherently permanent) and its unfavorable decision in Fox Photo, T.C. Memo 1990-348, (where the court found that "one-hour photo labs" located in shopping center parking lots were not inherently permanent).

[REDACTED]

[REDACTED]

If you have any further questions, please call the branch telephone number.

DEBORAH A. BUTLER
ASSISTANT CHIEF COUNSEL
(FIELD SERVICE)

By:

WILLIAM C. SABIN, JR.
SENIOR TECHNICIAN REVIEWER
Passthroughs and Special Industries
Branch
Field Service Division