



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

OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: DEBORAH A. BUTLER, ASSISTANT CHIEF COUNSEL (FIELD SERVICE)

CC:DOM:FS

SUBJECT:

Field Service Advice
Periodic Equipment Maintenance

This Field Service Advice responds to your memorandum dated April 21, 1999. It is not binding on Examination or Appeals and is not a final case determination. This document may not be cited as precedent.

LEGEND:

Taxpayer	=
Year 1, 2, 3	=
YY	=
XX	=
WW	=
VV	=
TT	=
\$Amount	=
\$\$Amount	=
\$\$\$Amount	=
\$\$\$\$Amount	=
\$\$\$\$\$Amount	=

ISSUES:

1. Whether Taxpayer should be required to capitalize the periodic costs it incurs to clean, sandblast, prime and paint certain barge hulls under I.R.C. § 263(a).
2. Whether costs incurred by Taxpayer to perform towboat engine maintenance in Years 1, 2 and 3 must be capitalized under section 263(a) or may those costs be deducted under section 162.
3. Whether in answering Issue 2 the analysis required by section 263 regarding material increases in value and life should be considered from the perspective of a composite asset only or should the towboat engines be considered separately from the towboats.

CONCLUSIONS:

1. Taxpayer is not required to capitalize its periodic costs to clean, sandblast, prime and paint certain barge hulls and it may claim a current business expense deduction for those costs under section 162.
2. Further case development is required.
3. Further case development is required.

FACTS:

This taxpayer--

runs full-service barge lines transporting various commodities on the inland waterway system in the United States. It has a fleet of towboats which it uses to propel its barges along the system. The barges in issue have an expected useful life of about YY to XX years; however, that life can arguably be extended to up to WW years by more frequent painting.

Maintenance of the barges includes sandblasting, priming and painting the barges' hulls to fight corrosion and natural deterioration. Painting and/or cleaning, if needed, is scheduled after regular inspection of the hulls. Based on Taxpayer's historical experience, although there is no set schedule, a barge is usually painted every VV to TT years.

The average cost of painting a barge usually depends upon whether it is a “tank” or “dry cargo” barge. A tank barge, with a replacement cost of about \$Amount, usually costs about \$\$Amount to paint. A dry cargo barge, with a replacement cost of about \$\$\$Amount, usually costs about \$\$\$\$Amount to paint. Taxpayer’s total annual cost for cleaning/painting averaged \$\$\$\$Amount for the years in issue.

LAW AND ANALYSIS:

Section 162 allows a deduction for all ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business. The regulations thereunder further provide that the costs of “incidental repairs” which neither materially add to the value of the property nor appreciably prolong its life—but keep the property in ordinarily efficient operating condition—may be currently deducted. Treas. Reg. § 1.162-4. That regulation also provides, however, that the cost of repairs in the nature of replacements that arrest deterioration and appreciably prolong the life of the property must be capitalized and depreciated in accordance with section 167. Id.

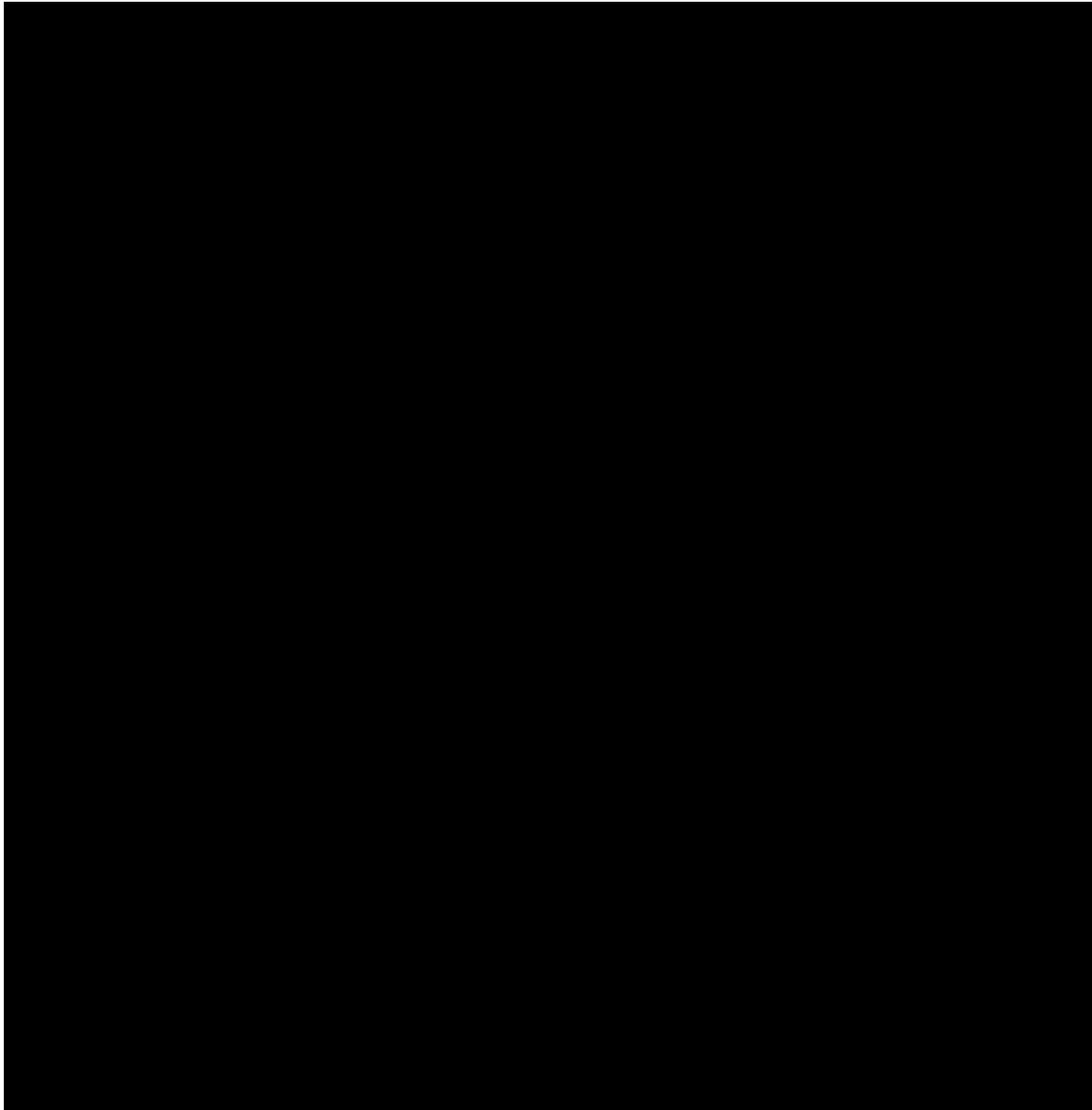
Section 263(a)(1) and Treas. Reg. § 1.263(a)-1(a) provide that no deduction is allowed for any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property. Moreover, section 263(a)(2) prohibits a deduction for amounts expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made. Treas. Reg. § 1.263(a)-1(b) specifically provides, however, that amounts paid or incurred for incidental repairs and maintenance within the meaning of section 161 and Treas. Reg. § 1.162-4 are not capital expenditures. Rev. Rul. 94-12, 1994-1 C.B. 36, makes clear that the Service’s position on the general deductibility of incidental repair and maintenance costs was unaffected by the Supreme Court’s decision in INDOPCO, Inc. v. Commissioner, 503 U.S. 79 (1992).

Notwithstanding the resultant incidental natural “prolonging” of the property’s useful life, the cost of painting a business or income-producing property has long been held deductible as an ordinary and necessary current expense. See, e.g., Haverty Furniture Co. v. Commissioner, 15 F.2d 345 (5th Cir. 1927).¹ Any

¹ Compare United States v. Wehrli, 400 F.2d 686 (10th Cir. 1968) (even if item is a repair standing alone, cost must be capitalized if part of general modernization or rehabilitation plan); Jones v. Commissioner, 57-1 U.S.T.C. ¶ 9517 (5th Cir.), aff’g 24 T.C. 563 (1955) (the cost of painting as part of remodeling plan is incidental to improvement and must be capitalized); Rev. Rul. 88-57, 1988-2 C.B. 36 (expenditures for major rehabilitations of railroad freight cars are capital under section 263(a)).

prolonged life in this case as a result of the cleaning/painting, is merely in the nature of an assumed maintenance of the inherent usefulness of the property. See Midland Empire Packing Co. v. Commissioner, 14 T.C. 635 (1950) (relining of basement wall to prevent oil seepage was merely to allow continued use of property for which it was intended); City National Bank v. Commissioner, No. 26610 (T.C. Memo. 1952), 11 T.C.M. (CCH) 411, 412-13 (cleaning, sandblasting and painting of building walls held deductible). Consequently, the cleaning, sandblasting, priming and painting of the barge hulls in issue here are currently deductible by Taxpayer.

CASE DEVELOPMENT, HAZARDS, AND OTHER CONSIDERATIONS:





By: _____
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