



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

OFFICE OF
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE LEGAL ADVICE

MEMORANDUM FOR VIVIANA TAVERNA
LMSB LM:F:MN

FROM: Associate Chief Counsel
(Passthroughs and Special Industries) CC:PSI:7

SUBJECT: Treatment of costs associated with a landfill

This Chief Counsel Advice responds to your memorandum. In accordance with § 6110(k)(3) of the Internal Revenue Code, this Chief Counsel Advice should not be cited as precedent.

LEGEND

Taxpayer =

Agency =

ISSUES

1(a). Whether taxpayer's costs for monitoring, maintenance and control activities associated with the closing of Phases I, VI and VII through X of its waste disposal landfill constitute qualified closing costs for purposes of computing the deduction for closing costs pursuant to § 468 of the Code? Taxpayer conducted its solid waste landfill operations for these phases pursuant to a permit issued by the Agency.

1(b). Whether taxpayer's costs for monitoring, maintenance and control activities associated with the closing of Phases II through V of its waste disposal landfill constitute qualified closing costs for purposes of computing the deduction for closing costs pursuant to § 468 of the Code? Taxpayer operated Phase II through Phase V under an Order on Consent, issued by the Agency after the filling of all but a small portion of Phase V was complete, but prior to the completion of the monitoring, maintenance and control activities associated with these phases.

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2. Whether the cost of liners required to be used in the taxpayer's landfill operations are depreciable assets or permanent improvements to the land? If it is determined that the liners are not permanent improvements, what is the proper amortization period of the liners?

CONCLUSIONS

1(a). The term "qualified reclamation and closing costs" as used in §468(d)(2)(B) of the Code includes amounts incurred after operations at a solid waste disposal site are terminated and the disposal site is covered or capped. The term "qualified closing costs" are those expenses incurred for any activity in connection with any solid waste disposal site that is conducted in accordance with any permit issued pursuant to the Solid Waste Disposal Act or any other Federal, State or local law. The maintenance, monitoring, and control activities required by the taxpayer's licenses and the applicable federal and state laws for Phases I, VI and VII through X are closing activities for the purpose of § 468(d)(2)(B).

1(b). We have insufficient facts to determine that the taxpayer was not acting within the requirements of section 468(d)(2)(B) of the Code.

2. While examination and the taxpayer agree that the liners are capital, we think you should seek assistance from CC:ITA on whether the costs are capital because of the similarity of this situation and the situation described in Rev. Rul. 94-28.

FACTS

For all audit years the taxpayer elected, pursuant to § 468, to deduct qualified reclamation and closing costs associated with its landfill operations. Examination adjusted taxpayer's claimed deductions for qualified reclamation and closing costs associated with the monitoring, maintenance and control activities (post-closing costs) of its landfill. It is Examination's position that the term "qualified closing costs" does not include expenses incurred after operations at a solid waste disposal site are terminated, and the disposal site is covered or capped.

In addition, under the state laws, the taxpayer was required to install a series of liners in the landfill site to prevent landfill debris leachate from leaking into the groundwater. The taxpayer amortized the liners over 5 years. The Service disallowed the taxpayer's amortization deduction on two alternative grounds. First, it is the Examination's position that the liners are not depreciable because they have no ascertainable useful life, since they are not biodegradable. If it is found that the liners are a depreciable asset, then Examination argues that the liners should be depreciated over 30 years, since the taxpayer is obligated to monitor the landfill site for 30 years after the site is closed.

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The property had been used for sand and gravel mining operations. In 1980, Taxpayer began carrying out mining operations on the property. In 1982, Taxpayer started filling operations on the mined out areas of the property.

Taxpayer received clean fill at the property, which is construction and demolition debris. Taxpayer received a fee for the filling operations. The filling operations of the mined out areas of the property were performed in accordance with requirements established by the Agency. Under Agency requirements, a landfill operator was required to underlay the area to be filled by at least two natural and/or synthetic liners, make provisions for leachate collection, have a treatment and disposal system approved by Agency, design, construct and operate gas recovery facilities, and provide monitoring, maintenance and control of the site for 30 years after the landfill site is closed.

The taxpayer's landfill operations were divided into Phases. Events regarding the landfill operations and the permits (or other written authorizations) issued to Taxpayer can be summarized as follows:

- Phase I. This phase consisted of acres. Taxpayer was issued a three year permit by Agency to operate a solid waste management facility on Phase I.
- Phases II through V. As filling in Phase I neared completion, application was made to the Agency, to expand the landfill by another acres, to be designated as Phase II. After discussions with the Agency, this application was amended on or about October 30, , to encompass an area of about acres, to be designated as Phases II through V. No permit, however, was ever issued by the Agency for Taxpayer to operate Phases II - V of the landfill.
- Although no permits were issued for Phases II through V, these phases were active and operating.
- Phase VI. Taxpayer applied for a permit from Agency to construct a acre site designated as Phase VI of its solid waste disposal facility. A permit was issued.
- The Agency addressed Taxpayer's landfill operations in Phases II through V by means of an Order on Consent that was negotiated with Agency while the hearing regarding the Phase VI permits was being conducted.

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- The Order on Consent was issued after the filling operations in phases II through V were nearly complete, but prior to the completion of the required monitoring, maintenance and control activities.
- In determining whether Taxpayer should be issued a permit for Phase VI, the Agency Commissioner reviewed the Order on Consent. This Order on Consent between the Taxpayer and Agency controlled all remaining aspects of the operation of Phases II through V, including the continued operation of Phase V and the closure of all four phases. Proper closure was ensured by a bonding requirement. During the hearing conducted to determine whether permits should be issued for phase VI, the Agency staff indicated that Taxpayer should be issued permits for Phase VI since the Consent Order addressed and resolved all issues that might otherwise have prevented permit issuance. The Agency found that although Phases II through V were operated in the absence of a permit, Taxpayer had been cooperative with the Agency and had operated the landfill in compliance with the operational requirements of the statutes.

In computing reclamation and closing cost deductions for its through tax years, the taxpayer included post-closure monitoring and maintenance costs for all phases of the landfill operations to be incurred over thirty years after a site is closed.

Liners

The Agency requires the maintenance of methane and drainage structures for a minimum of thirty years. An existing landfill must be underlain by at least two natural and/or synthetic liners, each with provisions for leachate collection, and have a treatment and disposal system that is approved by the Agency. The taxpayer assigned a five-year asset life to the liners and in began amortizing its cost of the liners using the straight-line method of depreciation.

LAW AND ANALYSIS

The Deficit Reduction Act of 1984 added section 468 to the Internal Revenue Code as an exception to the new economic performance requirement of section 461(h) and its regulations, which required a taxpayer on the accrual method of accounting to deduct expenses in the taxable year in which all the events had occurred that determine the fact of the liability and the amount of the liability with reasonable accuracy. Taxpayers electing the application of I.R.C. § 468 may deduct their reasonably estimated "qualified closing costs" of any closing activity in connection with any solid waste disposal site, prior to economic performance.

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Taxpayers not electing the application of I.R.C. § 468 are subject to the economic performance requirements imposed by I.R.C. § 461(h).

I.R.C. § 468(a)(1)(B) provides that the amount of any deduction for qualified closing costs for any taxable year shall be equal to the current closing costs allocable to the production from the reserve property during such taxable years. The term qualified closing costs is defined as any expense incurred for any closing activity in connection with any solid waste disposal site that is conducted in accordance with any permit issued pursuant to any Federal, State, or local law, which imposes requirements substantially similar to the requirements imposed by the Solid Waste Disposal Act. See I.R.C. § 468(d)(2)(B). The term "current closing costs" is defined as the amount that the taxpayer would be required to pay for qualified closing costs if the closing activities were performed currently. I.R.C. § 468(d)(1)(B)(i). The estimated closing costs, in the case of solid waste disposal sites, shall be computed on the unit-of-capacity method. I.R.C. § 468(d)(1)(B)(ii)(II).

The deduction for qualified closing costs for any tax year is equal to the current closing costs allocable to the production from a property during such tax year. I.R.C. § 468(a)(1)(B). Current closing costs are determined according to the unit-of-capacity method for solid waste disposal sites. I.R.C. § 468(d)(1)(B)(ii)(II).

Taxpayers electing the application of I.R.C. § 468 must add the amounts allowed as a current deduction under section 468 to either a reclamation reserve or closing cost reserve for the property, depending on the nature of the costs. I.R.C. § 468(a)(1)(B). Taxpayer has elected the application of section 468. There is no legal issue regarding the reserve balances.

Issue 1a.

The term "qualified reclamation and closing costs" as used in I.R.C. § 468(d)(2)(B) includes amounts incurred after operations at a solid waste disposal site are terminated and the disposal site is covered or capped (post-closure costs). Maintenance, monitoring, and control activities required by the taxpayer's licenses and the applicable federal and state laws may be closing activities for the purpose of I.R.C. § 468(d)(2)(B). Under I.R.C. § 468(d)(2)(B), the definition of the term "qualified closing costs" includes expenses incurred for any closing activity in connection with any solid waste disposal site that is conducted in accordance with a permit issued pursuant to any provision of a Federal or State law that imposes requirements substantially similar to the requirements imposed by the Solid Waste Disposal Act.

Under the Federal Resource Conservation and Recovery Act (which replaced the Solid Waste Recovery Act), the Environmental Protection Agency established

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national criteria for municipal solid waste disposal landfills to meet. Code of Federal Regulations Title 40, Part 258. The state rules incorporating federal guidelines and containing the permit application requirement, as well as the requirements for the design and operation of landfills and other solid waste facilities, are found in 6NYCRR Part 360-2. The federal requirements, include closure and post-closure criteria, which include installation and maintenance of the integrity of a final cover. During closure and post-closure, a landfill operator collects, monitors, treats and disposes of leachate, monitors the groundwater and the gas released from the solid waste disposal site, and maintains the monitoring and control equipment.

The term "qualified closing costs," defined in the statute as any expense incurred for any closing activity in connection with any solid waste disposal site conducted in accordance with any permit issued pursuant to any Federal or state law, includes the cost of post closure monitoring and maintenance activities.

Although decided on another issue, the court in South Side Landfill, Inc. v. United States, 52 F. Supp. 2d 783 (W.D. Mich. 1999) is supportive of our conclusion herein. The Second Circuit, to which this case is appealable, acknowledged that post closure obligations are required to be considered when computing the deduction pursuant to I.R.C. § 468. The court explained that post closure costs should be included to most accurately match income and expenses. It stated that I.R.C. § 468 allows landfill operators who use the accrual method of accounting to deduct a pro-rata portion of future closing and post-closing costs prior to economic performance. Id. at 786. Although the statement of the court in South Side Landfill is clearly dictum and not does not represent binding precedent, it does indicate that the Second Circuit considers post closure costs to be included in the calculation of qualified closing costs in order to accurately match income and expenses.

Issue 1b

The costs incurred and to be incurred by the taxpayer for closing phases II through V are costs that would have been incurred if the taxpayer had a permit. Whether the taxpayer was operating in compliance with the state permitting requirements is a matter of state law and, as there was no final finding by the state, it is unclear whether the taxpayer was or was not in compliance with the state law. We, therefore, have insufficient facts to determine that the taxpayer was not acting within the requirements of section 468(d)2(B) of the Code.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS

[REDACTED]

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While examination and the taxpayer agree that the liners are capital, we have not been able to get confirmation of this treatment from CC:ITA and therefore cannot determine what useful life, if any, is appropriate. You should send any information requests on this matter to CC:ITA.

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

Please call if you need further assistance please call Roger E. Baker at 622-3120 have any further questions.

By: _____
JOSEPH H. MAKURATH
Senior Technician Reviewer
Associate Chief Counsel
(Passthroughs and Special Industries)