

Internal Revenue Service

Department of the Treasury
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Person To Contact: _____, ID No.

Telephone Number:

Refer Reply To:
CC:ITA:B07
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Date:
August 23, 2013

Re: Request for Private Letter Ruling for Asset Classification under Section 168

Legend

- Taxpayer =
- City =
- Date =
- Year =
- x =
- y =

Dear

This letter responds to a letter dated February 27, 2013, and supplemental information dated June 24, 2013, submitted by Taxpayer requesting a ruling regarding the classification of certain interior, non-load bearing partitions for purposes of § 168 of the Internal Revenue Code.

FACTS

Taxpayer represents that the facts are as follows:

Taxpayer is an individual that uses the cash method of accounting and files his federal income tax returns on a calendar-year basis. Taxpayer’s business activities are that of a wholesale, retail, and leasing distributor of lighting and construction related products with associated administrative activities and professional engineering services, and a lessor of building space and the use of certain improvements.

Taxpayer plans to own a building with certain improvements containing approximately x square feet located in City (the “Owned Property”). This building is a rectangular two story facility with an entry lobby and central corridor in the middle of the long side of the rectangular building. The central corridor runs from the front parking lot

to the rear parking lot and connects an elevator tower on the front of the building with an enclosed fire stair tower on the rear to the building. Two additional exit fire stairs occur one at each end of the building along the short sides of the rectangle. Public restrooms and mechanical rooms feed off the central corridor.

Taxpayer anticipates initially occupying the Owned Property for use in its business. Further, Taxpayer is contemplating leasing a portion of, or all of, the Owned Property space with certain improvements to another party. Taxpayer anticipates to lease the Owned Property to the general public.

Further, Taxpayer leases from a third party approximately y square feet of space in a building in City (the "Leased Property"). Taxpayer has plans in place to remodel the Leased Property, including adding and paying for certain improvements. Taxpayer anticipates initially occupying the Leased Property for use in its business. Further, Taxpayer is contemplating sub-leasing all or a portion of Taxpayer's Leased Property to a sub-lessee. Taxpayer anticipates to sub-lease the Leased Property to the general public.

In completing the finish out of the Owned Property and in completing the remodeling and finish out of the Leased Property, Taxpayer anticipates purchasing, paying for, and depreciating two types of interior non-load bearing drywall partition systems: (i) a zip type drywall partition system and (ii) a conventional drywall partition system. Taxpayer will place in service both types of partition systems during the taxable year ending Date (the Year taxable year).

The zip type drywall partition system consists of the zip type partition elements that include zip type drywall partitions (i.e., removable/reusable gypsum drywall panels finished and painted), removable zip tape and joint compound, removable/reusable studs and tracks, and removable/reusable screws, and the zip type partition attachments that include removable/reusable panel coverings, removable/reusable base and crown trim, removable/reusable integral door units, removable/reusable internal utilities, removable/reusable integral glazing, and removable/reusable cabinets on the zip type drywall partitions. The zip type partition uses a releasable adhesive on the zip tape over the panel joint. Unlike other drywall joint tapes, a person can zip the zip tape up without the tape breaking even after the joint compound has significantly cured. When zipped up, the zip tape removes the joint compound that covers it and then exposes the screws under the zip tape in a manner that allows screw removal and then disassembly of the zip type partition for removal and re-use. A pull tab is on the zip tape to alert remodel contractors that this joint tape is the type that can be zipped up for disassembly of the partition.

The zip type partition is designed and constructed to be movable. It can be readily removed and can remain in substantially the same condition after removal as before, or it can be moved and reused, stored, donated, or sold in its entirety. Removal

of the zip type partition does not cause any substantial damage to the zip type partition itself or to the building. Taxpayer anticipates that the zip type partitions may need to be moved in order to accommodate the associated reconfigurations of the interior space within the Owned Property and Leased Property.

The conventional drywall partition system includes gypsum board partitions, studs, joint tape, and covering joint compound. The joint tape cannot be removed without breaking after the joint compound has had time to significantly cure. The removal of the joint tape and a conventional drywall partition can be easily accomplished only by demolition of the partitions. Disassembly or deconstruction of a conventional drywall partition in a manner that provides for easy reuse is not practical because the screws are beneath the non-removable joint tape and the covering joint compound.

The conventional drywall cannot be easily removed and cannot remain in substantially the same condition after removal as before, or it cannot be moved and reused, stored, donated, or sold in its entirety. Removal of the conventional drywall partition causes substantial damage to the partition itself but does not cause substantial damage to the building. Taxpayer anticipates installing conventional drywall partitions within the Owned Property and Leased Property in locations not subject to expansion, contraction, or reconfiguration.

Taxpayer also represents the following:

1. The zip type partitions to be placed in service during the Year taxable year are not inherently permanent structures under the factors described in Whiteco Industries, Inc. v. Commissioner, 65 T.C. 664, 672-673 (1975).

2. The conventional drywall partitions to be placed in service during the Year taxable year are inherently permanent structures under the factors described in Whiteco Industries.

RULINGS REQUESTED

Taxpayer requests the following rulings:

1. Taxpayer's zip type partitions installed within the Owned Property and Leased Property are included in asset class 57.0, Distributive Trades and Services, of Rev. Proc. 87-56, 1987-2 C.B. 674, as clarified and modified by Rev. Proc. 88-22, 1988-1 C.B. 785, for purposes of § 168.

2. Taxpayer's conventional drywall partitions installed within the Owned Property and Leased Property are classified as nonresidential real property under § 168(e)(2)(B).

LAW AND ANALYSIS

Section 167(a) provides a depreciation allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence) of property used in a trade or business or held for the production of income.

The depreciation deduction provided by § 167(a) for tangible property placed in service after 1986 generally is determined under § 168. This section describes two methods of accounting for determining depreciation allowances: (1) the general depreciation system in § 168(a); and (2) the alternative depreciation system in § 168(g). Under either depreciation system, the depreciation deduction is computed by using a prescribed depreciation method, recovery period, and convention.

For purposes of § 168(a) or 168(g), the applicable recovery period is determined by reference to class life or by statute. Section 168(i)(1) provides that the term “class life” means the class life (if any) that would be applicable with respect to any property as of January 1, 1986, under § 167(m) (determined without regard to § 167(m)(4) and as if the taxpayer had made an election under § 167(m)) as in effect on the day before the date of enactment of the Revenue Reconciliation Act of 1990. Prior to its revocation, § 167(m) provided that in the case of a taxpayer who elected the asset depreciation range system of depreciation, the depreciation deduction was based on the class life prescribed by the Secretary which reasonably reflects the anticipated useful life of that class of property to the industry or other group.

Section 1.167(a)-11(b)(4)(iii)(b) of the Income Tax Regulations sets out the rules for asset classification under former § 167(m). Property is included in the asset guideline class for the activity in which the property is primarily used. Property is classified according to primary use even though the activity in which such property is primarily used is insubstantial in relation to all the taxpayer’s activities.

Section 1.167(a)-11(e)(3)(iii) provides that in the case of a lessor of property, unless there is an asset guideline class in effect for lessors of such property, the asset guideline class for such property shall be determined as if the property were owned by the lessee. However, in the case of an asset guideline class based upon the type of property (such as trucks or railroad cars) as distinguished from the activity in which used, the property shall be classified without regard to the activity of the lessee.

Rev. Proc. 87-56 sets forth the class lives of property subject to depreciation under § 168. The revenue procedure establishes two broad categories of depreciable assets: (1) asset classes 00.11 through 00.4 that consist of specific assets used in all business activities; and (2) asset classes 01.1 through 80.0 that consist of assets used in specific business activities. The same depreciable asset can be described in both an asset category (that is, asset classes 00.11 through 00.4) and an activity category (that is, asset classes 01.1 through 80.0), in which case the item is classified in the asset

category. See *Norwest Corporation & Subsidiaries v. Commissioner*, 111 T.C. 105 (1998) (item described in both an asset and an activity category (furniture and fixtures) is placed in the asset category).

Asset class 57.0, Distributive Trades and Services, of Rev. Proc. 87-56 includes assets used in wholesale and retail trade, and personal and professional services. Asset class 57.0 also includes § 1245 assets used in marketing petroleum and petroleum products. Assets in this class have a recovery period of 5 years for purposes of § 168(a) and 9 years for purposes of § 168(g).

Section 168(e)(2)(B) defines the term “nonresidential real property” as meaning section 1250 property that is not residential rental property (as defined in § 168(e)(2)(A)), or property with a class life of less than 27.5 years. Nonresidential real property has a recovery period of 39 years for purposes of § 168(a) and 40 years for purposes of § 168(g).

Section 168(i)(12) defines the terms “section 1245 property” and “section 1250 property” as having the meanings given such terms by §§ 1245(a)(3) and 1250(c), respectively.

Section 1245(a)(3) defines the term “section 1245 property” as meaning any property that is or has been property of a character subject to the allowance for depreciation provided in § 167 and is either personal property or certain other property described within § 1245(a)(3)(B) through (F). See also § 1.1245-3(a). Section 1.1245-3(b) defines “personal property” as meaning tangible personal property as defined in § 1.48-1(c) (relating to the definition of “section 38 property” for purposes of the investment tax credit) and intangible personal property. Section 1.48-1(c) provides that “tangible personal property” means any tangible property except land and improvements thereto, such as buildings or other inherently structures (including items that are structural components of such buildings or structures).

Section 1250(c) defines the term “section 1250 property” as meaning any real property (other than section 1245 property, as defined in § 1245(a)(3)) that is or has been property of a character subject to the allowance for depreciation provided in § 167. See also § 1.1250-1(e)(1). Section 1.1250-1(e)(3) defines “real property” as meaning any property that is not personal property within the meaning of § 1.1245-3(b) and also provides that section 1250 property includes, among other things, a building or its structural components within the meaning of § 1.1245-3(c). Pursuant to § 1.1245-3(c)(2), the terms “building” and “structural components” have the meanings assigned to those terms in § 1.48-1(e).

Section 1.48-1(e)(2) defines the term “structural components” as including such parts of a building as walls, partitions, floors, and ceilings, as well as any permanent coverings therefore such as paneling or tiling; windows and doors; . . .

plumbing and plumbing fixtures, such as sinks and bathtubs; electric wiring and lighting fixtures; . . . sprinkler systems; . . . and other components relating to the operation or maintenance of a building.

The Senate Finance Committee, in S. Rept. No. 95-1263 (1978), 1978-3 C.B. 321, 415, issued in connection with the enactment of the Revenue Act of 1978, Pub. L. 95-600, 92 Stat. 2767, stated the following:

In addition, the committee wishes to clarify present law by stating that tangible personal property already eligible for the investment tax credit includes special lighting (including lighting to illuminate the exterior of a building or store, but not lighting to illuminate parking areas), false balconies and other exterior ornamentation that have no more than an incidental relationship to the operation or maintenance of a building . . . Similarly, . . . movable and removable partitions . . . are considered tangible personal and not structural components. Consequently, under existing law, this property is already eligible for the investment tax credit.

Rev. Rul. 75-178, 1975-1 C.B. 9, provides that the classification of property, such as movable partitions, as “personal” or “inherently permanent” should be made on the basis of the manner of attachment to the land or the structure and how permanently the property is designed to remain in place. This determination of permanency of the property, that is, whether the property in question is inherently permanent, is made by applying the factors set forth in Whiteco Industries, Inc. v. Commissioner, 65 T.C. 664, 672-673 (1975), acq., 1980-1 C.B. 1. No one factor is decisive. See JFM, Inc. and Subsidiaries v. Commissioner, T.C. Memo. 1994-239.

The Whiteco factors are: (1) Is the property capable of being moved, and has it in fact been moved? (2) Is the property designed or constructed to remain permanently in place? (3) Are there circumstances that tend to show the expected or intended length of affixation, that is, are there circumstances that show the property may or will have to be moved? (4) How substantial a job is removal of the property, and how time-consuming is it? (5) How much damage will the property sustain upon its removal? (6) What is the manner of affixation of the property to the land?

The depreciation classification of Taxpayer’s zip type partitions and conventional drywall partitions depends on whether the partitions are inherently permanent structures. This determination is made by the application of the Whiteco factors.

Zip type partitions

Taxpayer represents that the zip type partitions to be placed in service during the Year taxable year are not inherently permanent structures under the factors described in Whiteco Industries. This representation is a material representation. Based solely on

this representation, we conclude that the zip type partitions are tangible personal property for depreciation purposes.

During the Year taxable year, Taxpayer will place in service zip type partitions in buildings comprising the Owned Property and the Leased Property. Taxpayer anticipates initially occupying the entire Owned Property and Leased Property for use in its business. Taxpayer represents that its business activity is that of a wholesale, retail, and leasing distributor of lighting and construction related products with associated administrative activities and professional engineering services. Asset class 57.0 includes these business activities. Accordingly, the zip type partitions in the Owned Property and Leased Property are includible in asset class 57.0 when Taxpayer occupies the Owned Property and Leased Property for use in its business activity.

However, Taxpayer is contemplating leasing a portion of, or all of, the Owned Property space to another party. Further, Taxpayer is contemplating sub-leasing all or a portion of Taxpayer's Leased Property to a sub-lessee. Accordingly, the depreciation classification of the zip type partitions when used by the lessee(s) of the Owned Property or the sub-lessee(s) of the Leased Property depends upon the business activity of such lessee(s) or sub-lessee(s). See § 1.167(a)-11(e)(3)(iii).

Taxpayer anticipates to lease the Owned Property and to sub-lease the Leased Property to the general public. The business activity of leasing space in buildings to the general public is described in asset class 57.0 of Rev. Proc. 87-56. Accordingly, the zip type partitions in the Owned Property and Leased Property are includible in asset class 57.0 when Taxpayer leases the Owned Property and sub-leases the Leased Property to the general public.

Conventional drywall partitions

Taxpayer represents that the conventional drywall partitions to be placed in service during the Year taxable year are inherently permanent structures under the factors described in Whiteco Industries. This representation is a material representation. Based solely on this representation, we conclude that the conventional drywall partitions are structural components of the buildings comprising the Owned Property and Leased Property and, therefore, are classified as nonresidential real property under § 168(e)(2)(B).

CONCLUSIONS

Based solely on the facts and representations submitted, we conclude that:

1. Taxpayer's zip type partitions installed within the Owned Property and Leased Property are included in asset class 57.0 of Rev. Proc. 87-56 for purposes of § 168.

2. Taxpayer's conventional drywall partitions installed within the Owned Property and Leased Property are classified as nonresidential real property under § 168(e)(2)(B).

The rulings contained in this letter are based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter under any other provisions of the Code. Moreover, no opinion is expressed or implied as to: (i) whether Taxpayer's zip type partitions are not inherently permanent structures under the factors described in Whiteco Industries Inc.; (ii) whether Taxpayer's conventional drywall partitions are inherently permanent structures under the factors described in Whiteco Industries Inc.; (iii) whether Taxpayer has a depreciable interest in the zip type partitions or the conventional drywall partitions; or (iv) the proper asset class in Rev. Proc. 87-56 for the zip type partitions if Taxpayer leases the Owned Property or sub-leases the Leased Property to persons engaged primarily in one business activity.

This letter ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the power of attorney on file with this office, we are sending a copy of this letter ruling to Taxpayer's authorized representative. We also are sending a copy of this letter ruling to the appropriate operating division director.

Sincerely,

Kathleen Reed

Kathleen Reed
Branch Chief, Branch 7
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosures (2):
copy of this letter
copy of section 6110 purposes