

Action on Decision 1999-008

August 30, 1999

SUBJECT: Hospital Corp. of America and Subsidiaries v. Commissioner 109 T.C. 21 (1997).

Issue:

1. Whether the tests developed under the investment tax credit (ITC) prior to the 1981 adoption of the cost recovery system are applicable in determining a structural component for the purposes of Accelerated Cost Recovery System (ACRS) and Modified Accelerated Cost Recovery System (MACRS).
2. Whether certain items treated as tangible personal property and depreciated over a 5-year recovery period were in fact structural components of the buildings to which they relate which must be depreciated over the same recovery period as the buildings, pursuant to I.R.C. § 168.

Discussion:

On their tax returns for 1985 through 1988, the taxpayers classified as tangible personal property certain items in hospital facilities constructed in those years and took depreciation deductions for them using a 5-year recovery period. The property placed in service in 1985 and 1986 is subject to ACRS, while the property placed in service after 1986 is subject to MACRS. The Commissioner determined that the items were structural components of the hospital facilities and not tangible personal property and, therefore, should be depreciated over the same recovery period as the facilities to which they related.

In the Tax Court, the taxpayers argued that the items constituted section 1245 property, and, therefore, were appropriately depreciated using a 5-year recovery period. The Commissioner countered that allowing the items to be depreciated over a different recovery period than the buildings to which they related resulted in component depreciation, which is no longer allowed under ACRS and MACRS. The Commissioner also argued that ITC cases involving years prior to 1981, when the cost recovery system was adopted, are of limited application in determining what constitutes a structural component. Further, the Commissioner argued that section 168(f)(1) effectively operates to change the definition of tangible personal property after 1981, thereby precluding such property item from being classified as section 1245 property, [TEXT REDACTED] if it is attached to a building and has utility beyond its relation to a particular piece of property. It was the Commissioner's position that the items were structural components and thus section 1250 property and, therefore, should be depreciated over the same recovery period as the building to which they relate.

The Tax Court found that most of the assets at issue were section 1245 property. The Court rejected the Commissioner's primary argument stating that the test developed with respect to ITC and Treas. Reg. § 1.48-1(e) were inappropriate after the enactment of ACRS in 1981. The court concluded, after reviewing the statutory and regulatory language and case law, that, while Congress did prohibit the use of component depreciation, there was no intent to redefine section 1250 property under ACRS to include property that had been section 1245 property for purposes of the investment tax credit. Accordingly, the court held that, to the extent the disputed property would qualify as tangible personal property for the ITC under pre-1981 law, it will also qualify as tangible personal property for ACRS and MACRS.

The court also rejected the Commissioner's alternative argument that the disputed items were structural components under an ITC analysis. The court examined each category of disputed items to determine whether the assets should be characterized as section 1250 class property (a structural component of the facility) or section 1245 class property (tangible personal property under Treas. Reg. § 1.48-1(c)). In making this determination, the court looked to the factors delineated in *Whiteco Indus., Inc. v. Commissioner*, 65 T.C. 664, 672-673 (1975), to ascertain whether the items were inherently permanent and, thus, not tangible personal property within the meaning of Treas. Reg. § 1.48-1(c).

We acquiesce in this decision to the extent that the Tax Court held that the term "tangible personal property," as defined under a pre-1981 ITC analysis, has continued viability under ACRS and MACRS. The issue as to whether the various disputed items are structural components or tangible personal property is a factual question. We do not agree with the court's determination with respect to the various disputed properties. We cannot state, however, that the court was clearly erroneous. Thus, we could not recommend appeal. Cf. *Boddie-Noell Enterprises, Inc. v. United States*, 36 Fed. Cl. 722 (1996), *aff'd without op.* 132 F.2d 48, 35 F.T.C. 960 (Fed. Cir. 1997) (acoustical tile ceilings, a portion of an electrical system and a plumbing system were structural components under the regulations); *LaPetite Academy, Inc. v. United States*, 95-1 U.S.T.C. (CCH) 50, 193 (W.D. Mo. 1995) *aff'd without op.* 72 F.2d 132 (8th Cir. 1995) (wall panels, [TEXT REDACTED] kitchen plumbing, bathroom accessories and a portion of the electrical system were structural components under the regulations).

Recommendation:

1. Acquiescence.
2. Nonacquiescence.

Carolyn H. Gray, Trial Attorney

Reviewers:

Approved:

STUART L. BROWN, Chief Counsel

By: JUDITH C. DUNN, Associate Chief Counsel (Domestic)