APPEALS

INDUSTRY SPECIALIZATION PROGRAM

APPEALS SETTLEMENT GUIDELINES

INDUSTRY: GAMING / SHIPPING

ISSUE: CLASS LIFE OF FLOATING GAMING FACILITIES

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COORDINATED ISSUE
GAMING and SHIPPING INDUSTRIES

CLASS LIFE OF FLOATING GAMING FACILITIES
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STATEMENT OF ISSUE

Under the circumstances set out below, what are the appropriate asset classes and recovery periods of floating gaming facilities?

COMPLIANCE'S POSITION

The Compliance Coordinated Issue Paper provides a discussion of two different configurations of floating gaming facilities that are typical in the industry – casino riverboats and facilities positioned in moats.

The casino riverboat has a licensed crew and travels on United States waterways carrying passengers who engage in on-board gaming. The casinos which float in a moat are usually barges onto which a casino facility is built. The barges are located in a completely contained basin, isolated from any waterway.

The Coordinated Issue Paper concludes that the proper recovery period for the casino riverboat is described in asset class 00.28, Vessels, Barges, Tugs and Similar Water Transportation Equipment, with a recovery period of 10 years for purposes of IRC § 168(a) and 18 years for purposes of IRC § 168(g).

Since the facilities in a moat normally consist of barges that are an inextricable part of a multi-story, landlocked, gaming facility, and unlike the casino riverboat are permanently

moored and are no longer ready and available for operation as water transportation equipment, they should not be considered an asset described in asset class 00.28 - Vessels, Barges, Tugs and Similar Water Transportation Equipment. Instead, they should be treated as nonresidential real property for purposes of IRC § 168 with a recovery period of 39 years for purposes of IRC § 168(a) and 40 years for purposes of IRC § 168(g).

Depending on facts and circumstances, if a particular gaming facility is determined to be impermanent, it would be included in asset class 79.0, Recreation, rather than considered nonresidential real property. Assets used primarily in asset class 79.0 have a recovery period of 7 years for purposes of IRC § 168(a) and 10 years for purposes of IRC § 168(g). Also, consideration should be given as to whether any of the assets in this type of facility are included in asset class 00.3 - Land Improvements.

INDUSTRY / TAXPAYER POSITION

The industry position is that the population of floating casino facilities includes a diverse group of assets in both design and construction, and that the Coordinated Issue Paper, by focusing on the two limited fact patterns and using an analysis that focuses on whether the assets are a vessel or nonresidential real property, incorrectly leads one to conclude that the only possible recovery periods are 10 years or 39 years. They believe that this approach oversimplifies what should be a comprehensive analysis of factors used in determining whether a facility is real or personal property.

Typically, a taxpayer will consider its floating gaming facilities to be vessels with a recovery period of 10 years for purposes of IRC § 168(a).

DISCUSSION

Background

Taxpayers in the gaming industry include individuals, partnerships, corporations, and joint ventures operating gaming casinos on various facilities located in or near United States inland river waterways, river basins, channels, lakes, ponds, and cofferdams. These operations are conducted under licenses issued by local and state gaming agencies. Often, state law prohibits gaming on land-based facilities and requires that the gaming facilities be on water.

Floating casinos currently operate in states that have legalized riverboat gaming, including Mississippi, Louisiana, Missouri, Iowa, Illinois, and Indiana. Taxpayers operating these casinos conduct legalized gaming activities that include Blackjack, Poker, Roulette, Craps, Baccarat, Keno and Slot Machines. The gaming facilities are designed to attract gaming customers. In addition to the revenue from gaming, the gaming facilities derive revenue from food and beverage sales and entertainment. Most of the revenue is derived from gaming.

The Compliance Coordinated Issue Paper provides the two contrasting gaming facility fact patterns mentioned above – a casino riverboat and a casino facility in a moat. The paper provides an analysis of factors used to determine the proper asset class and recovery period for these facilities, and indicates that the methodology used to analyze these two types of facilities can be also applied to those facilities that are either permanently moored or located behind a cofferdam.

Facts relating to the casino riverboat

A casino operator either purchases or contracts with a U.S. shipyard to construct a U.S. flagged, self-propelled, marine vessel to be operated on the inland river waterways of

the United States, for the purpose of conducting gaming activities. The motorized vessel is registered and documented with either a state government agency or the U.S. Coast Guard. The vessel has been issued a Certificate of Inspection (COI) by the U.S. Coast Guard and carries passengers who engage in on-board gaming. The vessel is operated with a licensed crew and travels on United States waterways. The vessel has its own electric, water, sewage, and telecommunications systems, as well as a complete radar navigation system.

Facts relating to the gaming facility in a moat

A casino operator either purchases, or contracts with a U.S. shipyard to construct a barge or several barge units. The barges are towed to an interim river location. An inland channel or canal from the river to a water basin is dredged. The barges are towed into the water basin or they are built in place and various marine and land based contractors weld the barges together so that they will be a single welded structure. The number of barges used depends on the size of the structure permitted to operate under local and state government zoning requirements. The canal or channel is then backfilled so that the welded structure is completely isolated from the waterway.

The gaming facility is constructed by incorporating the welded structure as part of its foundation. After a layer of concrete is poured onto the common surface of the welded barges to create a level surface, a multi-story facility is constructed. The structure is held in place by hoists with cables that are anchored to the land with concrete caps on piles. Walls and a roof are then constructed around or attached over the welded structure. The gaming facility floats in a basin of water the depth of which is usually maintained by a pumping system. Although the facility has the appearance of a land-based casino, the fact that it is floating in the basin of water enables it to comply with local and state gaming laws. The gaming facility does not have its own independent electric, water, sewage, or telecommunications systems – land-based utilities provide those services. Additionally, it does not have a complete radar navigation system.

The gaming facility is constructed under the direction of a licensed contractor and requires approved zoning and building plans. The local city or county building authority grants the gaming facility a certificate of occupancy upon completion. Local government fire marshals monitor the gaming facility for maximum occupancy levels.

Legal Analysis

IRC § 167(a) provides a depreciation allowance for property used in a trade or business or held for the production of income. Property is eligible for the allowance when it is ready and available for a specifically assigned function. See Reg. § 1.46-3(d) and Reg. § 1.167(a)-10(b).

The depreciation deduction provided by IRC § 167(a) for tangible property placed in service after 1986 generally is determined under IRC § 168, which prescribes two methods for determining depreciation allowances. One method is the general depreciation system described in IRC § 168(a) and the other method is the alternative depreciation system described in IRC § 168(g). The depreciation deduction is computed under both systems by using a prescribed depreciation method, recovery period, and convention.

The applicable recovery period for purposes of either IRC § 168(a) or § 168(g) is determined by reference to class life. IRC § 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 former IRC § 167(m) as if it were in effect and the taxpayer were an elector under that section. Prior to its revocation, IRC § 167(m) provided that in the case of a taxpayer who elected the asset depreciation range system of depreciation, the depreciation deduction would be computed based on the class life prescribed by the Secretary that reasonably reflects the anticipated useful life of that class of property to the industry or other group.

Reg. § 1.167(a)-11(b)(4)(iii)(b) sets out the method for asset classification under former IRC § 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 use is insubstantial in relation to all of the taxpayer's activities.

Rev. Proc. 87-56, 1987-2 C.B. 674, sets forth the class lives of property used to compute the depreciation allowances under IRC § 168. Property that is neither described in an asset guideline class listed in section 5 of the revenue procedure, nor assigned a class life under IRC § 168(g)(3)(B), is treated as property having no class life. For purposes of the general depreciation system, IRC § 168(e)(3)(C) prescribes a 7-year recovery period for property with no class life, and for purposes of the alternative depreciation system, IRC § 168(g)(2)(C) prescribes a 12-year recovery period for property with no class life. [1]

The Standard Industrial Classification Manual (SIC) published by the Office of Management and Budget can provide insight into the content of the current asset classes described in Rev. Proc. 87-56. However, the SIC does not make use of the same classification techniques and depreciation concepts used in Rev. Proc. 87-56. While the SIC has precise categorization by primary business activity using language very similar to that found in Rev. Proc. 87-56, the revenue procedure departs dramatically from the categorization scheme of SIC by establishing 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 asset classes set out in Rev. Proc. 87-56 that are germane to the classification of the gaming facilities in each of the fact patterns are as follows:

[1] For purposes of this paper, it is assumed that the assets were placed in service before January 1, 1999. For property placed in service after December 31, 1998, the recovery period for regular income tax and for alternative minimum tax purposes is the same. IRC §168(a)(2)(C)(i) and §56(a)(1)(A)(i).

79.0 **Recreation**

Includes assets used in the provision of entertainment services on payment of a fee or admission charge, as in the operation of bowling alleys, billiard and pool establishments, theaters, concert halls, and miniature golf courses. Does not include amusement and theme parks and assets, which consist primarily of specialized land improvements or structures, such as golf courses, sports stadium, racetracks, ski slopes, and buildings which house the assets used in entertainment services.

Assets used primarily in asset class 79.0 have a recovery period of 7 years for purposes of IRC § 168(a) and 10 years for purposes of IRC § 168(g). The SIC category numbers for establishments engaged in operating various gaming devices and casino operations are 7993 and 7999, respectively. Asset class 79.0 includes gaming activities. The presumption in this paper is that the assets at issue are primarily used in gaming activities.

00.28 **Vessels, Barges, Tugs, and Similar Water Transportation Equipment, except those used in marine construction**

There is no further description for this class. Assets described in asset class 00.28 have a recovery period of 10 years for purposes of IRC § 168(a) and 18 years for purposes of IRC § 168(g). Any vessel, barge, tug, and similar water transportation equipment used as such primarily in the activity described in asset class 79.0 is classified in asset class 00.28.

00.3 **Land Improvements**

Includes improvements directly to or added to land, whether such improvements are IRC § 1245 property or IRC § 1250 property, provided such improvements are depreciable. Examples of such assets might include sidewalks, roads,

canals, waterways, drainage facilities, sewers (not including municipal sewers in Class 51), wharves and docks, bridges, fences, landscaping shrubbery, or radio and television transmitting towers. Does not include land improvements that are explicitly included in any other class, and buildings and structural components as defined in § 1.48-1(e) of the regulations. Excludes public utility initial clearing and grading land improvements as specified in Rev. Rul. 72-403, 1972-2 C.B. 102.

Assets described in asset class 00.3 have a recovery period of 15 years for purposes of IRC § 168(a) and 20 years for purposes of IRC § 168(g). Any land improvement used primarily in the activity described in asset class 79.0 is classified in asset class 00.3.

57.0 **Distributive Trades and Services:**

Includes assets used in wholesale and retail trade, and personal and professional services. Includes IRC § 1245 assets used in marketing petroleum and petroleum products.

This particular asset class was not mentioned in the Coordinated Issue Paper; however, some taxpayers in the industry have indicated that if their facilities are not vessels classified under asset class 00.28, then they would fall under this category.

Are the facilities "vessels?"

IRC § 7701(a) provides definitions for purposes of Title 26 (Internal Revenue Code) where not otherwise distinctly expressed or manifestly incompatible with the intent thereof. IRC § 7701(m)(1)(7) refers to 1 U.S.C. section 3 for the definition of "vessels." That section provides:

> The word "vessel" includes every description of watercraft or other artificial contrivance used, or capable of being used, as a means of transportation on water.

See also 46 U.S.C. section 2101(45).

A "barge" is a non-self-propelled vessel. 46 U.S.C. section 2101(2).

In some instances the courts have interpreted the term “vessel” broadly for purposes other than income tax. McCarthy v. Bark Peking, 716 F. 2d 130 (2nd Cir. 1983). However, the Supreme Court has denied vessel status to structures that have been withdrawn from navigation, such as crafts that have been laid up for the winter. Desper v. Starved Rock Ferry Co., 342 U.S. 187 (1952). See also Hawn v. American S.S. Co, 107 F. 2d 999 (2nd Cir. 1939). Also, where a converted gunboat was used as a museum and dance barge, it was not a vessel under 1 U.S.C. § 3. Hayford v. Doussony, 32 F.2d.605 (5th Cir. 1929). In this case the court relied on the fact that the converted facility was not used, nor was it intended to be used, to carry freight or passengers from one place to another, was not an instrument of navigation or commerce, and performed no function that might not have been performed as well by a floating stage or platform permanently attached to land.

In a recent series of decisions, courts have held that for purposes of the application of federal statutes, other than federal income tax statutes, dockside casinos are not vessels and state law is not determinative of a vessel's status for federal purposes. These cases are not controlling, but the rationale used by the courts is informative when considering whether an asset is a vessel.

In Biloxi Casino Belle Inc., 176 B.R. 427 (S.D. Miss 1995), the court held that the dockside casino was not a vessel even though the Coast Guard had previously documented it as such. The court noted that the Biloxi Belle had very few of the attributes commonly associated with a vessel. For example, it was not capable of

moving under its own power, was not seaworthy, had no crew concerned with vessel operations other than the activities relating to the casino, and had no standard maritime equipment such as navigational lights or lifesaving equipment. See also In the Matter of Treasure Bay, 205 B.R. 490 (S.D. Miss 1997); McAdow v. Promus Companies, Inc., 926 F.Supp. 93 (W.D. La 1996); King v. President Riverboat Casino-Mississippi, Inc., 894 F.Supp 1008 (S.D. Miss 1995) (the structure was, for all intents and purposes a land-based casino).

In Pavone v. Mississippi Riverboat Amusement Corp., 52 F.3d 560 (5th Cir. 1995), the Court of Appeals affirmed the District Courts for the Eastern District of Louisiana and the Southern District of Mississippi, holding that a floating dockside casino facility was not a vessel for purposes of the Jones Act, 46 App. U.S.C. section 688, or general maritime law. In its holding the court found three attributes common to non-vessels. The structure was built to be used primarily as a work platform; the structure was moored at the time of the accident; and although the platform was capable of movement, and was sometimes moved across navigable waters in the course of normal operations, any transportation was merely incidental to its primary purpose.

In King v. Grand Casinos of Mississippi, Inc., 697 So. 2d 439 (Sup. Ct. Miss. 1997), plaintiff argued that the dockside casino was a vessel because it was licensed as such under Mississippi state law. The Court indicated that the state statute did not determine the issue of vessel status under the federal Jones Act.

The U.S. Coast Guard Marine Safety Manual, Volume II paragraph 10. I. 1 (see also, 46 CFR 71.01-1 and 46 CFR 91.01-1), has a classification for "Vessels In Immobile Status" that includes "Permanently Moored Vessels". An abstract of the Safety Manual states, in pertinent part, the following:

I. Vessels in Immobile Status.

1, Permanently Moored Vessels.

(a) Introduction. A floating fuel dock, showboat, theater, hotel, restaurant, museum, etc., is not a "vessel" for inspection purposes if it is permanently moored and thus taken out of navigation. In this manner, the entity is "substantially a land structure" and not subject to the inspection laws. However, it may be subject to other regulations, such as those promulgated under the Ports and Waterways Safety Act (PWSA). The following criteria should be used in determining whether an entity is "substantially a land structure."

(1) It must be securely and substantially moored as approved by the U.S. Coast Guard Office in Charge of Marine Safety (OCHI).

(2) The mooring must be so rigged that its lines cannot be inadvertently or accidentally cast off, it is unlikely to break away from its mooring, and it cannot be moved away from the mooring without special effort (i.e., the use of tools).

(3) Permanent connection to shore side facilities is evidence of being a "land structure". The nature and use of the entity may also be considered.

(b) Change in Use.

A vessel may be placed in navigation periodically, yet keep its status as "substantially a land structure" when moored. When returned to navigation, it becomes subject to inspection under the regulations applicable to its particular operation. The owner or operator must notify the U.S. Coast Guard, Office of Marine Inspection, prior to placing the vessel in navigation. When the vessel is again immobilized, the U.S. Coast Guard, Office of Marine Inspection, must approve the mooring arrangement before the vessel can be considered "permanently moored." Once these conditions are met, the vessel would again be considered out of navigation. This procedure is intended to allow the "permanent" mooring of a vessel that is placed in navigation on a regular basis (e.g., weekly or monthly trips between ports). When intended operations are tantamount to use as a vessel normally requiring inspection,

claims of status as substantially a land structure are voided and the structure must be inspected and certified. [Note: Local authorities should be advised whenever a vessel's status is changed to "substantially a land structure", so that appropriate civil safety codes may be applied.]

The Coordinated Issue Paper included a list of factors which are helpful in determining whether an asset is “otherwise ready and available” for use as an asset described in asset class 00.28. This listing has also been included in these guidelines as Exhibit A.

As stated in the Coordinated Issue Paper, the discussion above leads to the conclusion that the casino riverboat that regularly cruises during its operation belongs under asset class 00.28, Vessels, Barges, Tugs and Similar Water Transportation Equipment, because during the taxable year it was certified by the U.S. Coast Guard and was otherwise ready and available, within the meaning of IRC § 168 of the Code, to operate as a vessel in the casino operator's business. Consequently, the casino riverboat has a recovery period of 10 years for purposes of IRC § 168(a) and 18 years for purposes of IRC § 168(g). This conclusion will likely be noncontroversial. However, should the casino riverboat lose its certification or otherwise fail to be ready and available as an asset described in asset class 00.28 for any taxable year, the asset would be subject to the change-in-use rules of IRC § 168(i)(5).

For facilities placed in a moat or basin, the Coordinated Issue Paper concludes that unlike the casino riverboat, the barges are permanently moored within the meaning of the Marine Safety Manual and are no longer ready and available for operation as water transportation equipment. Thus, the gaming facility is not an asset described in asset class 00.28, Vessels, Barges, Tugs and Similar Water Transportation Equipment.

If the facility does not fall under this classification, then what is the proper asset class for this type of facility?

Classifying facilities as nonresidential real property or personal property

If a facility does not qualify as a "vessel," the next question is whether it should be classified as some other form of tangible, personal property, or whether it is nonresidential real property.

IRC § 1245(a)(3) states, in pertinent part, that section 1245 property is any property of a character subject to the allowance for depreciation under IRC § 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 in connection with a qualified activity,
(c) a single purpose agriculture or horticultural structure, or
(d) a storage facility used in connection with the distribution of petroleum.

Under Reg. § 1.48-1(c) and § 1.48-1(d), tangible personal property is defined in part as "any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures (including items which are structural components of such buildings or structures)."

If a facility is properly classifiable as nonresidential real property, then its recovery period is statutorily prescribed. The recovery period is 39 years for purposes of IRC § 168(a), and 40 years for purposes of IRC § 168(g).[2] IRC § 168(e)(2)(B) defines "nonresidential real property" as IRC § 1250 property which is not residential rental property or property with a class life of less than 27.5 years.

IRC § 168(i)(12) provides that "section 1250 property" has the same meaning as IRC § 1250(c), which provides that IRC § 1250 property is any real property, other than IRC §

[2] The cost of nonresidential real property is recovered under the straight-line method over a recovery period of 39 years for property generally placed in service after May 12, 1993 (IRC § 168(c)(1)). For nonresidential real property generally placed in service after 1986 and before May 13, 1993, cost is

1245 property, which is or has been of a character subject to the allowance for depreciation provided in IRC § 167. Pursuant to Reg. § 1.1245-3(c)(2), the terms "buildings" and "structural components" shall have the meanings assigned to those terms in IRC § 1.48-1(e). A building is defined in Reg. § 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. Such term includes any such structure constructed by or for a lessee even if such structure must be removed or ownership of such structure reverts to the lessor at the termination of the lease.

Factors to consider in determining whether a structure is a building include inherent permanency, the appearance of the structure, and the function of the structure. See L.L. Bean, Inc. v. Commissioner, T.C. Memo 1997-175, aff'd. 145 F.3d 53 (1st Cir. 1998). In this case, the Tax Court, citing Treas. Reg. § 1.48-1(e)(1), stated that the appearance test for a building generally requires a structure enclosing space within its walls and covered by a roof. The function test is whether the structure provides working space for employees which is more than merely incidental to the primary function of the structure. In determining whether a structure is inherently permanent, the Tax Court set forth six factors to consider in Whiteco Industries, Inc. v. Commissioner, 65 T.C. 664, 672-73 (1975). These factors are:

(1) Is the property capable of being moved, and has it in fact been moved? Alabama Displays, Inc. v. United States, 507 F.2d 844 (Ct. Claims 1975); Moore v. Commissioner, 58 T.C. 1045, 1052 (1972), aff'd. per curium 489 F.2d 285 (5th Cir. 1973);

(2) Is the property designed or constructed to remain permanently in place? Weirick v. Commissioner, 62 T.C. 446, 451 (1974); Everhart v. Commissioner, 61 T.C. 328 (1973); Roberts v. Commissioner, 60 T.C. 861, 866 (1973);

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recovered under the straight-line method over a recovery period of 31.5 years. The mid-month convention is applicable.

(3) Are there circumstances, which tend to show the expected or intended length of affixation, i.e., are there circumstances, which show that the property may or will be moved? Alabama Displays, supra; LaCroix v. Commissioner, 61 T.C. 471 (1974);

(4) How substantial a job is removal of the property and how time consuming is it? Is it readily removable? Estate of Shirley Morgan v. Commissioner, 52 T.C. 478 (1969) aff'd. 448 F.2d 1397 (9th Cir. 1971);

(5) How much damage will the property sustain upon its removal? King Radio Corp. v. United States, 486 F.2d 1091, 1096 (10th Cir. 1973); and

(6) What is the manner of affixation of the property to the land? Weirick, supra; Everhart, supra; Roberts, supra.

In L.L. Bean, supra, the taxpayer contended that even if its facility resembled and functioned as a building, it was not an improvement to land because it was movable. The court stated that proper application of the Whiteco factors rests on the premise that movability itself is not the key determinant of lack of permanence, and the mere fact that the taxpayer's facility could theoretically be moved did not establish that it was not inherently permanent. In finding that the taxpayer's facility was inherently permanent the court noted that the facility was specifically designed for the site as an addition to taxpayer's distribution center and that the time and effort involved to move the facility would be substantial. With regard to another asset at issue in L.L. Bean, supra, the Mezzanine System (system), the court found that the taxpayer's building was planned and designed with the integration of the system in mind and concluded that the substantial time and effort involved in both the construction and potential removal of the system, as well as the degree of its integration with the building, reflected the permanent nature of the system.

By contrast, the Tax Court in Fox Photo Inc. v. Commissioner, T.C. Memo. 1990-348, determined that one-hour photo labs, usually located in shopping center parking lots, and containing a retail area, a film development area, and a storeroom, qualified as tangible personal property and were therefore eligible for the investment tax credit. The Court concluded that even though the labs had the appearance of buildings, they were readily movable, and unlike the usual building, were constructed in anticipation of the possibility that they may have to be moved. Lease provisions allowed the taxpayer to terminate a site in the event of "economic adversity" and required that the labs be moved upon expiration of the fixed term of the lease or other termination. However, the Court determined that the concrete foundations for the labs were immovable and inherently permanent and did not qualify for the investment tax credit.

The Court came to this conclusion despite the fact that the labs had an estimated useful life of 50 years, the petitioner intended to leave the labs on their original sites for an indefinite period of time, and the petitioner conceded that the labs were buildings under the appearance and function test in Reg. § 1.48-1(e). In reaching its conclusion, the Tax Court focused on whether the labs were "inherently permanent," noting that in cases in which the issue of movability has been involved, they approached the question of whether property was a "building" by determining whether the structure was inherently permanent. The Court noted that in Moore v. Commissioner, 58 T.C. 1045, (1972), aff'd. 489 F.2d 285 (5th Cir. 1973), it held that since the regulations cite "buildings or other inherently permanent structures" as examples of improvements to land, to fit the definition of a building an item of property (in this case trailers) must be an inherently permanent structure on the land. The Moore opinion also stated that the functional use test is not the sole criterion to determine the status of an item of property; rather, before the functional use test could be used in that case, the trailers at issue must first be shown to be permanent improvements to the land. Following that rationale, the Court in Fox Photo applied the Whiteco factors to reach the following conclusions about the photo labs:

· The labs were capable of being moved and were constructed so that they could be moved (some were in fact moved subsequent to the years at issue in the case).

· The manner of affixation did not add to the element of permanency associated with the usual building.

· The fact that the petitioner stipulated that it intended to leave the labs at their original locations did not require a different conclusion. The Court found that the lease termination provisions due to "economic adversity," and the requirement that the labs be moved at the expiration of the lease showed that the labs might have to be moved, and were in fact moved.

· The labs could be moved in 12 to 18 hours, requiring five men to work 2 to 3 days, sustaining damage that was less costly to repair than building a new lab.

· Movability alone does not decide the issue; they determined whether the labs were readily movable and constructed in anticipation of being moved, unlike the usual building.

Rev. Ruling 75-178, 1975-1 C.B. 9, held that:

> The use of a functional or equivalency test (1) to classify property as inherently permanent where it is not itself physically attached to the land, or (2) to classify property as a structural component where it is not an integral part of (and therefore a permanent part of) a building, is no longer the criteria to be used to classify property. Rather, the problem of classification of property 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.

The revenue ruling held that floating docks that are not attached to land are tangible personal property. This same issue was considered in Estate of Shirley Morgan, supra, wherein the Tax Court determined that floating docks were not inherently permanent when they were not themselves driven into the bed of the bay. In this case, the

Government argued that the docks were inherently permanent structures because they are permanently attached or affixed to land by three methods:

1. Attached by gangways which are hinged to permanent piers on shore and rollers.
2. Connection rollers – connection of electrical and plumbing utilities from land-based sources.
3. Attachment of the docks to pilings.

The Court, which personally inspected the docks, determined that the docks float as independent units, rising and falling with the tide. The pilings only limit lateral motion of the docks. The docks are portable. The gangways merely rest on the docks by means of rollers. Electrical and plumbing connections are not significantly different from those of ships and boats which depend on land-based utilities when the vessels are docked. The Court did not believe that using pilings to guide the docks converted them into permanent fixtures. The pilings were not an integral part of the docks. They are used to serve the same purpose as anchors attached to cables. The fact that the docks functioned the same as those that are attached to land did not make them inherently permanent structures. The pilings were, however, found to be inherently permanent structures because they were affixed to the land. The Court also found it important that the docks were readily movable, although it did not discuss the time, effort and cost required to move them.

When evaluating whether a facility is personal or real property, consideration of the "law of fixtures" may prove useful. Over the years, the courts have grappled with the concept of personal property shedding its identity as personalty and assuming the status of real property or fixtures. Fixtures have been defined as a species of property lying along the dividing line between real and personal property; as objects which were originally personal property but which, by reason of their annexation to or use in association with real property, have become a part of the realty. (35 Am Jur 2d Fixtures @ 1). The general tests for determining whether a particular object has become a fixture are usually said to comprise annexation to the realty, adaptation to the use to

which the realty is devoted, and intention that the object become a permanent accession to the freehold. There is some disagreement, however, on the relative importance to be assigned the foregoing factors as between themselves. At early common law, annexation to the soil was the fundamental test for determining whether the object had assumed the character of a fixture. Later courts took the position that the paramount consideration was whether the object and the realty were so adapted or interrelated that the one would be relatively useless without the other. There seems to be general agreement today that annexation is no longer a matter of controlling importance, and some courts hold that intention is the chief factor, while others take the position that all things should be declared fixtures which are attached to the land in furtherance of the purpose for which it is used. A widely accepted view is that the united application of all three tests is required, but it is evident that even this will not suffice in all situations and that there are other factors, including the relationship of the claiming parties, the relative difficulty of removal, the nature of the article annexed, and whether the fact of annexation is open and apparent, which will be considered in appropriate cases. (35 Am Jur 2d Fixtures @ 4).

How does the "law of fixtures" apply to the floating casino issue? A review of the law for the particular state in which a floating casino facility is located may be a resource for consideration. There may be pertinent case law which sheds light on whether assets such as a floating gaming facility could possibly be considered part of the realty, e.g., local or state taxing authorities may tax the facility as realty. Although not controlling, some research into the particular state's treatment of fixtures may prove useful in your analysis of the issue.

The Coordinated Issue Paper concludes that the barge facilities in the "boat in a moat" type configuration are used as an inextricable part of a multi-story, landlocked, gaming facility used primarily in the business activity described in asset class 79.0, Recreation. Unlike the casino riverboat, the barges are permanently moored and no longer ready and available for operation as water transportation equipment, thus they are not assets described in asset class 00.28, Vessels, Barges, Tugs and Similar Water Transportation

Equipment. The fact that the gaming facility is permanently moored within the meaning of the applicable U.S. Coast Guard rules is not, by itself, determinative that the facility is an inherently permanent structure for depreciation purposes. Whether the gaming facility is inherently permanent is determined by application of the Whiteco factors. A gaming facility that is determined to be an inherently permanent structure that meets the definition of a building found in Reg. § 1.48-1(e), and satisfies the criteria of appearance and function cited by the Court in L.L. Bean, supra, would be classified as nonresidential real property under IRC § 168, since asset class 79.0, Recreation, does not include buildings.

The Coordinated Issue Paper applied the Whiteco factors to the "boat in a moat" type gaming facility and concludes that it is an inherently permanent structure. The manner of its attachment to the land, which incorporates concrete and steel pilings, and the sheer size of the multiple-floor structure indicate that there is no intent to move the gaming facility. Further, in view of the length of the backfilled canal, any movement of the facility to another site (assuming permits could be obtained) would be prohibitively time consuming and expensive. (Compare and contrast Fox Photo and L.L. Bean.)

Furthermore, the gaming facility encloses space within its walls, is covered by a roof, and provides workspace. Accordingly, it meets the definition of a building provided by Reg. § 1.48-1(e) of the regulations. It also looks like and functions as a building, satisfying the criteria discussed by the court in L.L. Bean, supra. The gaming facility functions as a casino and is always located in the same place. Therefore, the Coordinated Issue Paper concludes that the gaming facility is nonresidential real property for purposes of IRC § 168, and has a recovery period of 39 years for purposes of IRC § 168(a) and 40 years for purposes of IRC § 168(g). The paper does note, however, that if upon application of the Whiteco factors a particular gaming facility is determined to be impermanent, the gaming facility would be an asset described in asset class 79.0, Recreation, rather than nonresidential real property.

Under Reg. § 1.1250-1(e)(2), § 1.1245-1(c), and § 1.48-1(e)(2), a building includes its structural components. Thus, any property that is enclosed within or attached to a gaming facility that is nonresidential real property must be analyzed to determine if the property is a structural component of the gaming facility. In addition to those items specifically set out in § 1.48-1(e)(2), structural components include any permanently attached item that is not considered machinery and equipment. For a gaming facility that meets the "boat in a moat" configuration, any property item that is not a structural component would be tangible personal property described in asset class 79.0, Recreation (unless it is a specific depreciable asset, described in asset classes 00.11 through 00.4, that is used in all business activities). See Hospital Corporation of America, 109 T.C. 21 (1997), acq, 1999-52 I.R.B. 763; Cf. Boddie- Noell Enterprises, Inc. v. United States, 36 Fed.Cl. 722 (1996) aff'd without op. 132 F.3d 54 (Fed. Cir. 1997); 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.3d 133 (8th Cir. 1995).

The Coordinated Issue Paper also notes that some of a facility's assets might belong in asset class 00.3, Land Improvements. These assets include IRC § 1250 property and other inherently permanent IRC § 1245 property. Thus, any casino facility that does not qualify as nonresidential real property because of its impermanence would likewise fail to be described in asset class 00.3. However, some of the assets located at the facility site might be permanently attached to the land, similar to the examples set out in asset class 00.3, such as wharves and docks. These assets might also be used in conjunction with a riverboat casino operation. Such assets have a 15-year recovery period for purposes of IRC § 168(a) and a 20-year recovery period for purposes of IRC § 168(g).

The same law and analysis would apply to other configurations of floating gaming facilities. Two other configurations which are frequently encountered are (1) the facility in a cofferdam, in which a gaming facility can be constructed in or moved to a site on or adjacent to a river and confined in the cofferdam, or (2) a gaming facility that is substantially moored to a wharf or pier. In each instance, the analysis would entail

considerations of whether the gaming facility had been permanently moored and removed from navigation under the applicable U.S. Coast Guard rules and whether the gaming facility is inherently permanent within the meaning of the Whiteco factors. Consideration should be given to the relative costs of the water-based and land-based facilities. (Where the cost of land-based facilities greatly exceeds the cost of water-based facilities it is unlikely that the water-based facilities would be moved, even if such movement were theoretically possible). In addition, in some instances it may be appropriate to make use of the integrated structure analysis discussed by the court in L.L. Bean, supra, in the permanency determination.

SETTLEMENT GUIDELINES

As stated in the Coordinated Issue Paper, an intense factual analysis on a case-by-case basis is required for each variation of floating gaming facility. An on-site visit to see exactly how the facility has been placed and moored at the site, and how it has been integrated with the surrounding land based facilities, would be useful. For this reason, an Appeals Officer assigned this issue would benefit from physically viewing the facility, if feasible. If a visit is not feasible, the file should contain a comprehensive set of photographs showing not only the detail of the facility and its moorings, but also an overview of the area to show the land based facilities that have been built in conjunction with the casino facility, and how the casino has been integrated into the other facilities. In many instances, the facilities built around the casino are extensive and costly, and are only economically feasible due to the presence of the casino. The examination report should include photographs, as well as a complete description of the facility. The description should include the manner in which it was constructed and the design and cost to place it in its location.

A WORD OF CAUTION to an Appeals Officer visiting a facility- the visitation should be done either independently, or with Compliance personnel ONLY if the taxpayer is also present or has been invited to attend, in order to avoid a perceived violation of the ex parte rules contained in Rev. Proc. 2000-43, 2000-2 CB 404.

The Coordinated Issue Paper discusses only two of the possible configurations in any detail, and even within each configuration there could be substantial differences between facilities. Nonetheless, the facilities are normally considered to be placed within one of four general configurations:

1) The casino riverboat that normally cruises on the waterway.
2) The facility that is located on a waterway but is permanently or substantially moored to the land or a land improvement.
3) The facility which is confined to a cofferdam.
4) The “boat in a moat” that is confined to a basin and is essentially landlocked.

Depending on the facts, a facility could be placed in one of the following asset classes:

- Class 00.28 - Vessels, barges, tugs, and similar water transportation equipment, with a cost recovery period of 10 years under the general depreciation method;
- Class 00.3 - Land improvements, with a cost recovery period of 15 years;
- Class 79.0 - Recreation property with a cost recovery period of 7 years; or
- Nonresidential real property with a recovery period of 39 years.

A taxpayer may claim that the facility belongs in asset class 57.0, Distributive Trades and Services, with a cost recovery period of 5 years, but since the primary activity is gaming, such classification is unlikely. It also appears unlikely that the facilities would be considered property with no class life, since the primary activity of a gaming facility is described in asset class 79.0 – Recreation, which includes assets used in the provision of entertainment services. However, asset class 79.0 specifically excludes buildings which house the assets used in entertainment services. Thus, the issue will likely focus on whether the gaming facility at issue can be classified as a vessel, placing it in asset class 00.28, even though its primary activity is gaming, or, if it is not a vessel, is it recreation property in asset class 79.0, or are some or all of the assets land improvements described in asset class 00.3.

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RELATED CONSIDERATIONS / ISSUES

A change to correct a taxpayer's consistently used improper method, recovery period, or convention for computing the taxpayer's depreciation deductions is a change to the taxpayer's method of accounting, subject to the provisions of IRC §§ 446 and 481 and the regulations thereunder. Also note that if a floating casino facility is depreciated as non-residential real property, the possible impact on the alternative minimum tax should be considered.

Exhibit A

Some factors for determining whether a floating gaming facility is ready and available for use as an asset described in asset class 00.28.

Registered with U.S. Coast Guard or similar governmental authority.

Certified by the Coast Guard as a seaworthy vessel.

Periodically surveyed by a shipping classification society, such as the American Bureau of Shipping (ABS) with the classification "active".

Designed by a marine architect.

Built in a shipyard and not by a general contractor.

A "Plimsoll" or loadline welded onto the hull where the water line is located.

Carries life Preservers.

Qualifies for section 7518 Marine Capital Construction Fund (CCF) Administered by Maritime Administration (MARAD).

Qualified for a Title XI guarantee mortgage by MARAD.

Self-propelled and maintains its own independent utilities, such as electric, water and sewage system.

Propelled by motorized vessels (Pushed or Towed).

Has an independent navigation system.

Communication is generally ship to shore.

Employees are required to have specific active types of licenses and are certified for such positions as ship captain, 1st officer, radio officer, engineer officer 1st mate, etc.

Certain functions require U.S. Coast Guard Stamps (i.e.-taking on fuel on a vessel require persons in charge, Red Baker flag must be flown while bunkering the vessel).

Document charter parties are covered under marine admiralty law.

Insurance of shipboard employees is under Jones Act Trade.

Carries hull and marine insurance issued by an Inland Marine Underwriters Association.

On mortgaged vessels there are certain assurances regarding the mortgage such as the "Preferred Ship Mortgage Act of 1920."

Flies a flag of the nation in which the vessel is registered.