

INTERNAL REVENUE SERVICE

Index Numbers: 47.02-01

47.02-06

Number: **199934014**

Release Date: 8/27/1999

CC:DOM:P&SI:6--PLR-103216-99

May 28, 1999

LEGEND:

Taxpayer =

Parent =

City =

Building =

a =

b =

c =

d =

e =

f =

g =

h =

i =

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Dear

This letter is in response to a letter dated January 11, 1999, and a subsequent submission, from your authorized representative requesting a letter ruling under sections 38 and 47 of Internal Revenue Code in regard to the rehabilitation of a building.

Taxpayer represents that the facts are as follows:

Taxpayer is a member of the Parent's affiliated group. Parent files a consolidated federal income tax return and is under the jurisdiction of the district director in City.

Taxpayer owns the Building, which is a a story structure placed in service in b. It is basically a rectangular shaped building with a central light and air well. This light and air well is designed solely to bring light and air into the center of the Building, is completely surrounded by external walls of the Building, encloses space that is not designated for occupancy or use by people (other than possibly for maintenance or emergency), and runs from floor c to floor a. The lower floors of the Building are completely enclosed throughout the total space of the Building from the external walls inward.

Taxpayer has applied for registration of the Building on the National Register of Historic Places and expects the application to be approved.

Taxpayer is renovating the Building for numerous business purposes, including life safety, building maintenance, and building improvements. The major items of rehabilitation include roof replacement, construction of a new exit stair, construction of new restrooms that comply with the Americans with Disabilities Act (ADA), installation of a fire alarm system and a fire sprinkler system, replacement of heating, ventilation, and air conditioning system, electrical upgrades, construction of full floors in the light and air well from floor i to floor a, and window replacement. Seventy-five percent or more of the existing internal structural framework will be retained.

The "fill-in" of the light and air well will provide the space to house the new exit stair, mechanical shafts, and the electrical and communications rooms to be located on various floors. The remainder of the space will be "finished out" to provide additional rentable floor space.

The current adjusted basis of the Building, including tenant improvements, is less than \$d. The rehabilitation expenditures are estimated to range from \$e to \$f. The rehabilitation is planned to take place in phases over a time period in excess of g

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months but less than h months. Distinct phases have been identified by the architects, and written plans, describing all phases of the rehabilitation process, have been included with the request for ruling.

The rehabilitation expenditures will be depreciated as nonresidential real property over a 39 year period using the straight line method of depreciation.

The Building is not tax-exempt use property within the meaning of section 168(h) of the Code.

Section 38(a) of the Code provides for a general business credit composed of, in part, the current year business credit. Section 38(b)(1) provides that the current year business credit includes the investment credit determined under section 46. For purposes of section 38, section 46 provides that the amount of the investment credit for any taxable year is the sum of the rehabilitation credit, energy credit, and reforestation credit.

For purposes of section 46 of the Code, section 47(a) provides that the rehabilitation credit for any taxable year is the sum of (1) 10 percent of the qualified rehabilitation expenditures with respect to any qualified rehabilitated building other than a certified historic structure, and (2) 20 percent of the qualified rehabilitation expenditures with respect to any certified historic structure.

Section 47(c)(1)(A) of the Code defines the term "qualified rehabilitated building" as meaning any building (and its structural components) if (i) such building has been substantially rehabilitated, (ii) such building was placed in service before the beginning of the rehabilitation, (iii) in the case of any building other than a certified historic structure, in the rehabilitation process 50 percent or more of the existing external walls of such building are retained in place as external walls, 75 percent or more of the existing external walls of such building are retained in place as internal or external walls, and 75 percent or more of the existing internal structural framework of such building is retained in place, and (iv) depreciation is allowable with respect to such building.

Section 47(c)(1)(C)(i) of the Code provides that, for purposes of section 47(c)(1)(A)(i), a building is treated as having been substantially rehabilitated if the qualified rehabilitation expenditures during the 24-month period selected by the taxpayer (at the time and in the manner prescribed by regulation) and ending with or within the taxable year exceed the greater of the adjusted basis of the building (and its structural components) or \$5,000.

Section 47(c)(1)(C)(ii) of the Code provides a special rule for phased rehabilitation if the rehabilitation is expected to be completed in phases set forth in written architectural plans and specifications completed before the rehabilitation begins.

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In such a case, "60-month period" is substituted for "24-month period" in section 47(c)(1)(C)(i).

Section 47(c)(2)(A) of the Code defines "qualified rehabilitation expenditures" as any amount properly chargeable to capital account (1) for property for which depreciation is allowable under section 168 and is nonresidential real property, residential rental property, or real property with a class life of more than 12.5 years, and (2) in connection with the rehabilitation of a qualified rehabilitated building.

Section 47(c)(2)(B)(iii) of the Code excludes any expenditure attributable to the enlargement of an existing building from the definition of qualified rehabilitation expenditures.

Section 1.48-12(c)(10)(i) of the Income Tax Regulations provides that, in general, a building is enlarged to the extent that the total volume of the building is increased. The total volume of a building is, in general, equal to the product of the floor area of the base of the building and the height from the underside of the lowest floor (including the basement) to the average height of the finished roof. For this purpose, floor area is measured from the exterior faces of external walls (other than shared walls that are external walls) and from the centerline of shared walls that are external walls. Section 1.48-12(c)(10)(i) further provides that an increase in floor space resulting from interior remodeling is not an enlargement of a building.

Section 1.48-12(b)(3)(ii) of the regulations defines "external wall" as including any wall that has one face exposed to the weather, earth, or an abutting wall of an adjacent building. Further, this regulation provides that in general, the term "external wall" includes only those external walls that form part of the outline or perimeter of the building or that surround an uncovered courtyard. The walls of an uncovered internal shaft, designed solely to bring light or air into the center of a building, that are completely surrounded by external walls of the building and that enclose space not designated for occupancy or other use by people (other than for maintenance or emergency) are not considered external walls. Thus, for purposes of section 1.48-12(b)(3)(ii), the walls of a light well that is in the center of a building and not usable by people (other than for maintenance or emergency) are not external walls.

Section 1.48-12(b)(3)(iv) of the regulations provides, in part, that an external wall is retained in place notwithstanding that the existing doors and windows in the wall are modified, eliminated, or replaced.

Section 47(c)(2)(B)(iv) of the Code provides that the term "qualified rehabilitation expenditure" does not include any expenditure attributable to the rehabilitation of a certified historic structure or a building in a registered historic district, unless the rehabilitation is a certified rehabilitation. For this purpose, section 47(c)(2)(C) defines the term "certified rehabilitation" as meaning any rehabilitation of a certified historic

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structure that the Secretary of the Interior has certified to the Secretary as being consistent with the historic character of such property or the district in which such property is located.

The term "certified historic structure" is defined in section 47(c)(3)(A)(i) of the Code and section 1.48-12(d)(1)(i) of the regulations as meaning any building (and its structural components) that is listed in the National Register of Historic Places ("National Register").

Accordingly, based solely on the representations and relevant law set forth above, we rule that:

1. The "60-month period" special rule for phased rehabilitation provided in section 47(c)(1)(C)(ii) of the Code applies in determining whether the Building has been substantially rehabilitated within the meaning of section 47(c)(1)(C)(i).
2. All rehabilitation expenditures relating to the Building that are described in the ruling request and properly chargeable to capital account qualify as qualified rehabilitation expenditures for purposes of section 47 of the Code.
3. Provided the rehabilitation is certified by the Secretary of the Interior as a certified rehabilitation within the meaning of section 47(c)(2)(C) of the Code, Taxpayer is eligible for the rehabilitation credit under section 47(a)(2) with respect to the qualified rehabilitation expenditures made to the Building as a certified historic structure.

No opinion is expressed or implied regarding the application of any other provisions of the Code or regulations.

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

A copy of this ruling should be attached to the federal income tax return of the Taxpayer for the taxable year in which the rehabilitation tax credit is properly taken.

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In accordance with the power of attorney on file, a copy of this letter ruling is being sent to your authorized representatives. A copy of this letter ruling is also being sent to the District Director,

Sincerely yours,

Kathleen Reed  
Kathleen Reed  
Senior Technician Reviewer  
Branch 6  
Office of Assistant Chief  
Counsel  
(Passthroughs and Special  
Industries)

Enclosures (2):  
copy for 6110 purposes  
copy for federal tax return