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The Great Section 38 Property Muddle

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NOTES

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I. INTRODUCTION

The world of investment credit is a shadow land where the natural laws of reality function only erratically: it is a land where barns are buildings but henhouses and silos are not, where easily transportable objects are transformed through strange metaphysics into inherently permanent structures. Much of the property in this mysterious and seldom explored area of the law is "section 38 property" and therefore eligible for the credit, but the search for the characteristics serving to distinguish this elect property from less favored assets may seem at times as fruitless as the quest for the Philosopher's Stone.

II. BACKGROUND

A. *Basic Concept and Policy*

The 1962 Revenue Act[1] created the Investment Credit by adding section 38(a) to the Internal Revenue Code of 1954. That section tersely provides that "[t]here shall be allowed, as a credit against the tax imposed by this chapter, the amount determined under subpart B of this part." Section 46(a) limits the amount of the credit in most cases to 7 per cent of the "qualified investment."[2] The credit was enacted to stimulate the expansion of the economy, reflecting a desire, as outlined in the President's 1962 Economic Report, to

1. Revenue Act of 1962, Pub. L. No. 87-834, 76 Stat. 960 (codified in scattered sections of 26 U.S.C.).

2. The "qualified investment" is described in INT. REV. CODE OF 1954, § 46(c) as the aggregate of the "applicable percentage of the basis of . . . new section 38 property" placed in service during the taxable year, plus the "applicable percentage of the cost of . . . used section 38 property" placed in service during that year.

The "applicable percentage" varies from a minimum of 33 1/3% for property with a useful life of 3 to 5 years to 100% for property with a useful life of 7 years or more.

Unlike most other property, "public utility property" is limited to a 4% credit. This property is defined as that used "predominantly in the trade or business of the furnishing . . . electrical energy, water, or sewage disposal services, . . . gas . . . or communications services" in section 46(c)(3)(B).

increase the profitability of productive investment by reducing the net cost of acquiring new equipment.[3] Investment in capacity expansion and modernization is encouraged by the credit in order to spur an increase in production and output, thereby enhancing the competitiveness of American exports in world markets.[4] A strong medicine for a flagging economy, the credit has been interrupted during periods of boom to relieve inflationary pressures.[5] The credit was restored in its present form[6] by the 1971 Revenue Act;[7] it is estimated that the credit saves business—and thereby costs the Treasury—some four billion dollars annually.[8] Thus the Commissioner's attitude toward allowance of the credit is not always noteworthy for expansive munificence.

B. Important Definitional Elements

Section 46(c) limits the credit to "section 38 property." This crucial concept is defined in section 48(a)(1):

> *In general.*— Except as provided in this subsection, the term "section 38 property" means—
> (A) tangible personal property, or
> (B) other tangible property (not including a building and its structural components) but only if such property—
>
> (i) is used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or
> (ii) constitutes a research facility used in connection with any of the activities referred to in clause (i), or
> (iii) constitutes a facility used in connection with any of the activities referred to in clause (i) for the bulk storage of fungible commodities (including commodities in a liquid or gaseous state), or
>
> (C) elevators and escalators . . .
>
> . . . .
>
> Such term includes only property with respect to which depreciation (or amortization in lieu of depreciation) is allowable and having a useful life (determined as of the time such property is placed in service) of 3 years or more.[9]

3. H.R. REP. No. 1447, 87th Cong., 2d Sess., 1962-3 CUM. BULL. 405, 411 [hereinafter cited as 1962 REPORT]. Because the language of the Senate Report is virtually identical, reference will be only to the House Report.

4. *Id.*

5. The credit was suspended in 1966, restored in 1967, suspended again in 1969, then restored again in 1971. Eisner, *Business Investment Preferences*, 42 GEO. WASH. L. REV. 486, 489 (1974).

6. Among the changes introduced by the 1971 restoration were a shortening of the required useful life for property to be credited from 4 years to 3, and the substitution of the more precise phrase "a facility . . . for the bulk storage of fungible commodities (including commodities in a liquid or gaseous state)" for the rather vague term "storage facilities" in section 48(a)(1).

7. Revenue Act of 1971, Pub. L. No. 92-178, 85 Stat. 497 (codified in scattered sections of 26 U.S.C.).

8. Eisner, *supra* note 5, at 490 n.16.

9. INT. REV. CODE of 1954, § 48(a)(1).

This definition appears deceptively simple; in fact, the determination of what is and what is not "section 38 property" is of labyrinthine complexity and subtlety. There have been over 100 published revenue rulings and judicial decisions on the issue, characterized chiefiy by their ad hoc nature, conclusory reasoning, and, all too often, inconsistency *inter se*. Congress' original mandate[10] that words be given their ordinary meaning has become overgrown with a thicket of tangled and often confiicting fictions.[11]

Mindful that words may not mean what they seem to in the twilight zone of the investment credit, we now examine the essential concepts of section 48's definition of "section 38 property." The first requirement for property to qualify is that it be depreciable, with a useful life of more than three years.[12] Within that framework almost all[13] "tangible personal property" qualifies for the credit. "Tangible personal property" is defined[14] in terms of that which it is not: all property that is not intangible, and that is neither land nor an improvement thereto such as buildings and other inherently permanent structures; all property in the nature of machinery is specifically included as tangible personal property.[15]

In addition, "other tangible property"—basically, realty and improvements—may qualify for the credit. In order to qualify, however, this "other tangible property" must fall into one of four broad categories relating to its function. The first category is property used "as an integral part of manufacturing, production, or extraction. . . ." The second qualifying class is other tangible property used "as an integral part . . . of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services" by one engaged in the trade or business of furnishing such services.[16] A

10. TECH. EXPLANATION OF H.R. REP. No. 1447, 1962-3 CUM. BULL. 503, 515. [Hereinafter cited as 1962 TECH. EXPLANATION].

11. Compare the statement of 1962 TECH. EXPLANATION that " 'building' is to be given its commonly accepted meaning" with the recent Court of Claims rejection of any resort to the dictionary definition of "building." Brown-Forman Distillers Corp. v. United States, 74-2 U.S. Tax Cas. ¶ 9592, at 84,911 (Ct. Cl. 1974).

12. As noted earlier, this requirement was revised downward in 1971 from four years. *See* note 6 *supra*.

13. Section 48(a) excludes: most property used outside the United States except as specifically provided in subsection 48(a)(2)(B); property used predominantly for the furnishing of lodging, although property used by hotels and motels may qualify for the credit; property used by certain tax-exempt organizations; property used by governmental organizations; horses (but not other livestock); property completed abroad or of predominantly foreign origin; certain amortized property; and certain railroad track. INT. REV. CODE OF 1954, § 48(a)(2)-(9).

14. *See* note 35 *infra* and accompanying text.

15. *See generally* Treas. Reg. § 1.48-1(c) (1975).

16. This requirement is not found in section 48, but was apparently imported by the regulations from the description of "public utility property" in section 46(c)(3)(B).

third subdivision of qualifying "other tangible property" consists of "research facilities used in connection with any of the activities . . . [specified in either of the preceding categories]." The fourth type of qualifying "other tangible property" is composed of facilities "for the bulk storage of fungible commodities,"[17] subject to the same use restrictions as "research facilities." Though "buildings" and their "structural components" might appear to be the paradigm examples of "other tangible property," they *never* qualify as section 38 property.[18] Finally, elevators and escalators (which are beyond the scope of this paper) also qualify if installed after June 30, 1963.

C. The Fundamental Conflict and Resultant Confusion

From the taxpayer's point of view, the most desirable characterization for his property is "tangible personal property," because that property is subject to neither the "integral part" nor "in connection with" restrictions on use. Predictably, the Commissioner has sought to constrict the reach of "tangible personal property" while expanding the nonqualifying categories of "buildings" and their "structural components." Between the ultraviolet of tangible personal property and the infrared of buildings on the property spectrum, there is ample room for skirmishing over the nature of an "inherently permanent structure," the meaning of an "integral part of" "manufacturing, production, or extraction," the characteristics of "storage facilities," or the existence of a bona fide "trade or business" should the property at issue be involved in the furnishing of electricity, water, or other service activities.

The employment of so many terms of art naturally makes for very dense semantic undergrowth in this area. Moreover, the Committee reports specifically provided that local law should not be the controlling definitional source.[19] Unfettered by state law, the Commissioner's broad power to promulgate the regulations under which the credit is to be administered[20] provides him with a distinct advantage in the struggles over the characterization and interpretation of section 38 property. The Service has the definitional power to

17. The original enactment merely referred to "storage facilities." Revenue Act of 1962, Pub. L. No. 87-834, 76 Stat. 960 (codified in scattered sections of 26 U.S.C.). There is some controversy over the extent to which this 1971 change of diction really changed the law. *See* text following note 186 *infra*.

18. The problem of distinguishing between nonqualifying "buildings" and "facilities for bulk storage" or other "inherently permanent structures," which do qualify, will be discussed at length. *See* text following note 159 *infra*.

19. *See* 1962 REPORT, *supra* note 3, at 415.

20. INT. REV. CODE OF 1954, § 38(b) provides:

"(b) *Regulations.*—The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this section and subpart B."

create a semantic framework providing wide space for maneuvering between various tests it creates, and has so employed this power. Not all of the tests formulated by the regulations and rulings seem entirely consistent with one another;[21] indeed, on occasion the Service has been apprehended by the courts in the embarrassing act of taking a position directly contradicting an earlier position.[22] Sadly, neither are the courts innocent of the sin of inconsistency.[23]

Although it may be dangerously premature to speak of trends in an area as factually oriented as the definition of section 38 property, it seems fair to conclude on balance that, in categorizing an item of property for investment credit purposes, both the Commissioner and the courts are placing increasing emphasis on a consideration of the item's function rather than its forms and appearance. There is much to recommend this sort of approach: it may provide a better clue than does appearance for ascertaining whether an item is "in the nature of machinery," and, as the law has developed, it is the only way to distinguish a qualifying storage facility from a nonqualifying warehouse. But there are also difficulties with an increased emphasis on function: an improper mix of considerations in a close case may lead to a conclusion that a structure which to the common understanding is a building is, nevertheless, not a "building" in the statutory sense because of some peculiar function, thus giving rise to a technical and fictitious distinction. Additionally, there are situations in which a strict functional approach may produce a plainly inappropriate result, such as the characterization of a temporary metal room divider as a structural component by comparing its function to that of a wall, totally ignoring the absence of the important attribute of permanence.[24] Thus it is an oversimplification to conclude, as some have done, that a bare functional analysis can provide all the answers to the perplexing questions lurking within the definition of section 38 property.

In addition to the pervading inconsistencies of interpretation and dispute over the proper place of "function," the third major problem in the area is with lacunae in the regulations. By and large, the network of interrelating concepts in the definitional regulation

21. For example, in the area of "buildings" the Service has frequently zig-zagged between an appearance test and a functional approach, whichever seemed more advantageous, on the apparent assumption that it is more difficult to hit a moving rationale. *See* note 215 et seq. *infra* and accompanying text.

22. Minot Fed. Sav. & Loan Ass'n v. United States, 435 F.2d 1368, 1370-72 (8th Cir. 1970). *Compare* Joseph B. Weirick, 62 T.C. 446 (1974) *with* Beverly R. Roberts, 60 T.C. 861 (1973).

23. *Compare* Robert E. Catron, 50 T.C. 306 (1968) *with* Merchants Rofrigerating Co., 60 T.C. 856 (1973) *and* Palmer Olson, 1970 P-H Tax Ct. Mem. ¶ 70,296.

24. *See* text accompanying note 49 *infra*.

provides satisfactory interfaces at the points where those concepts touch or stand as exceptions to one another. Nevertheless, there are some gaps where concepts such as "in the nature of machinery" cut across "inherently permanent structure," "building," and "tangible personal property."

III. "TANGIBLE PERSONAL PROPERTY"

A. *Legislative History and Regulations*

If property is identified as "tangible personal property," it qualifies as section 38 property regardless of its use or the nature of the taxpayer's activity. The Code does not define tangible personal property, yet this is probably the largest class of items qualifying as section 38 property. The House Ways and Means Committee Report for the 1962 Revenue Act[25] indicates that the term "is not intended to be defined narrowly . . . nor to necessarily follow the rules of state law."[26] Therefore the vagaries and complexities of the local law of fixtures are not to be controlling:

> It is intended that assets accessory to a business such as grocery store counters, printing presses, individual air-conditioning units, etc., even though fixtures under local law, are to qualify for the credit. Similarly, assets of a mechanical nature, even though located outside a building, such as gasoline pumps, are to qualify for the credit.[27]

The language of the Senate Report is identical.[28] This language plainly indicates that tangible personal property is to be defined more broadly for the investment credit than for purposes of local law. The Technical Explanations to the Committee Reports[29] state that tangible personal property includes any tangible property except land and improvements thereto, such as buildings or other "inherently permanent structures" and the "structural components" of such buildings or structures.[30] The Technical Explanations add "transportation or office equipment, refrigerators . . . testing equipment, display racks and shelves" to the enumerated examples of assets accessory to the operation of a business.[31] The same section, describing items "in the nature of machinery" (a slight, but, significant,[32] change of diction from "of a mechanical

25. 1962 REPORT, *supra* note 3, at 405.
26. *Id.* at 415.
27. *Id.* at 415-16.
28. S. REP. No. 1881, 87th Cong., 2d Sess., 1962-3 CUM. BULL. 707, 722.
29. 1962 TECH. EXPLANATION, *supra* note 10, at 515.
30. *Id.* at 515-16.
31. *Id.*
32. For example, it is doubtful that the argument over the status of the line towers mounting pulleys and sheave assemblies at a ski lift would have arisen in *Weirick* had the

nature") includes hydraulic car lifts and gasoline pumps as examples. Intangibles, such as patents and copyrights, do not qualify.[33]

The regulation's basic definition of tangible personal property[34] amplifies the Committee Reports and Technical Explanations:

> [T]he term "tangible personal property" means 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). . . . Tangible personal property includes all property (other than structural components) which is contained in or attached to a building.[35]

But whereas the Committee Reports' statements that local law should not be controlling seem to have been intended to broaden the scope of tangible personal property by liberating it from state fixture law,[36] the regulations make plain that the concept's independence from local law cuts both ways:

> Local law shall not be controlling for purposes of determining whether property is or is not "tangible" or "personal." Thus, the fact that under local law property is held to be personal property or tangible property shall not be controlling.[37]

Further, while the regulation supplies few additional examples of the sort of property which *does* qualify as tangible personal property,[38] it is quick to list numerous illustrations of nonqualifying property: swimming pools, paved parking areas, wharves and docks, bridges and fences. The Service's clear purpose is to restrict the scope of tangible property.

B. Classes of "Tangible Personal Property"

(1) Items Contained in or Attached to a Building

The most prolific class of tangible personal property is "property (other than structural components) which is contained in or attached to a building."[39] The first revenue ruling[40] dealing with

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language of the regulations been "mechanical" rather than "machinery." For a fuller discussion of this case, see notes 62-65 *infra* and accompanying text.

33. 1962 TECH. EXPLANATION, *supra* note 10, at 516.

34. Treas. Reg. § 1.48-1(c) (1975).

35. *Id.*

36. *See* notes 26 & 27 *supra* and accompanying text.

37. Treas. Reg. § 1.48-1(c) (1975). The regulations do concede, however, that "property may he personal property for purposes of the investment credit even though under local law the property is considered to be a fixture and therefore real property." *Id.* It is significant that this concession follows, rather than precedes, the *in terrorem* remark that the Service does not feel bound by a local determination that property is personalty.

38. In addition to those items in the text following note 30 *supra*, the regulations mention only neon signs and automatic vending machines. *Id.*

39. *See* note 35 *supra* and accompanying text.

40. Rev. Rul. 65-79, 1965-1 CUM. BULL. 26.

section 38 property adopted a rather cooperative position on what would and would not be excluded from tangible personal property because a "structural component." Responding to a query from a bank, the Service declared that bank vault doors, night depository facilities, and both walk-up and drive-up tellers' windows would be considered tangible personal property and thus eligible for the credit. The Service reasoned that because all of the aforementioned property could be removed without affecting the bank's operation "as a building," the property must perforce be "equipment," rather than "structural components."[41] Further, since these specialized doors and windows were commonly used throughout the banking industry, "they must be considered as items accessorial to the conduct of the banking business, and therefore 'tangible personal property.' "[42]

This first approach, basically asking "does the property relate to the general functions common to all buildings (lights, etc.), or to the specialized activity carried on in *this* building (bank vault doors, tellers' windows and other 'accessorial' items)," was subsequently applied to find that the seats in a baseball stadium were tangible personal property in Revenue Ruling 69-170.[43] The Service there observed that although the stadium was a "building," the seats were: "neither essential parts of the 'building', nor [were] they items that relate to the operation or maintenance of the building. Rather, they relate to the operation of the taxpayer's business of presenting [baseball] . . . ."[44] For the same reasons, the flagpole, backstop, scoreboard, and message board mounted at various points on the same structure qualified as tangible personal property, by analogy to the example in the regulations of neon signs mounted on buildings.[45] This rather liberal test has not been universally applied, however;[46] indeed, that ruling marked its last public appearance.

Another key for distinguishing tangible personal property contained in a building from the structural components thereof is the relative permanence of attachment to the building.[47] Revenue Rul-

41. *Id.* at 27-28.

42. *Id.* at 28.

43. 1969-1 CUM. BULL. 28.

44. *Id.*

45. The ruling went on to draw a most unconvincing distinction between items attached to the stadium and identical items which happened to be set in the ground inside the stadium, terming the latter equipment "inherently permanent structures." *Id.* at 29. *See* text accompanying note 98 *infra*.

46. *See, e.g.*, Rev. Rul. 74-3, 1974 INT. REV. BULL. No. 1, at 11 (enclosures for inventoried parts in a warehouse); Rev. Rul. 68-405, 1968-2 CUM. BULL. 35 (extra-heavy insulation).

47. This factor is also a key consideration in identifying an "inherently permanent

ing 67-349[48] concluded that wall-to-wall carpeting installed in certain areas of a motel could qualify for the credit as tangible personal property. Unlike paneling permanently attached to a wall, the carpet was neither an integral part of nor permanently affixed to the floor, and was not therefore a structural component. In its zeal to control the credit, however, the Service for a time moved away from this eminently reasonable approach, replacing the stress on permanence with an emphasis on analogy of use: if the item performs the same function as a structural component, then it should be considered one (the argument went) regardless of its lack of permanence.[49] This "analogy of function" test has met with a uniformly inhospitable reception in the courts,[50] and the Service has recently shown signs of abandoning it for a return to the "permanence" analysis.[51]

(2) Items "in the Nature of Machinery": A Troublesome Ambiguity

Building from the statement in the Committee Reports that items of a "mechanical nature"[52] are to be considered tangible personal property, the regulations include items "in the nature of machinery" as qualifying tangible personal property, whether attached to a building or affixed to the ground. Examples of such property are the pumps and portable sprinkling equipment for a golf course,[53] and certain equipment for washing the movable windows at a racetrack grandstand.[54] In *Hayden Island, Inc.*,[55] a semiportable sewage treatment plant was held to be tangible personal property because of its mechanical nature, and because it was designed to be moved from place to place without great difficulty.[56]

Because the regulations characterize "inherently permanent structures" not as tangible personal property but as "other tangible

structure." It was several years before this rather basic conclusion was reached, however. *See* note 102 *infra* and accompanying text.

48. 1967-2 CUM. BULL. 48, 49.

49. *See, e.g.*, Rev. Rul. 69-14, 1969-1 CUM. BULL. 26 (movable partitions are "structural components").

50. *See* King Radio Corp. v. United States, 73-2 U.S. Tax Cas. ¶ 9766, at 82,481 (10th Cir. 1973); Minot Fed. Sav. & Loan Ass'n v. United States, 435 F.2d 1368 (8th Cir. 1970).

51. *See* Rev. Rul. 74-391, 1974 INT. REV. BULL. No. 33, at 6 (emphasizing the permanence of a wood-block floor in denying the credit).

52. 1962 REPORT, *supra* note 3, at 416.

53. Rev. Rul. 69-273, 1969-1 CUM. BULL. 30. This ruling denied the credit for the pipe and valve system, however. *See* note 80 *infra* and accompanying text.

54. Rev. Rul. 69-614, 1969-2 CUM. BULL. 8. The credit was denied, though, for the equipment that *raised* the windows.

55. 74-2 U.S. Tax Cas. ¶ 9604 (D. Ore. 1974).

56. The water and sewer lines connected to the treatment machinery were held to be "other tangible property," however. *Id.* at 84,944.

property,"[57] what should be the result when an item "in the nature of machinery" is also "inherently permanent"? Is it tangible personal property, or other tangible property? The regulations do not address this problem, and the Service skirted it in Revenue Ruling 69-169.[58] That ruling held the cable support towers[59] of a ski lift were inherently permanent structures, and thus other tangible property, but the Service did not mention any mechanical characteristics of the towers. In *Beverly Roberts*,[60] however, the ambiguity was presented more squarely. The property in question was the massive steel tower of an amusement ride known as the "Astro-Needle." At the top of the tower there was machinery for hoisting and rotating an observation gondola. The Commissioner convinced the Tax Court that even if the Astro-Needle were regarded as a type of machinery, its status as an inherently permanent structure prevented it from qualifying as personal property.[61]

The issue soon arose again in *Joseph B. Weirick*,[62] in which the taxpayer contested the conclusion in Revenue Ruling 69-169[63] that ski lift support towers were nonqualifying "other tangible property" because of their inherently permanent status.[64] The Commissioner had conceded during the course of the litigation that the drive and tension towers at either end of the lift, even though "inherently permanent," could qualify as tangible personal property because they were also "in the nature of machinery"; nevertheless, he maintained that the support towers between the terminals were not of that nature despite the inconvenient fact that the support towers housed certain pulley apparatus necessary for the operation of the lift. The Tax Court noted the inconsistency between the concession that the terminal towers were personal property regardless of permanence, and the position taken the year before in *Roberts* that "permanence" controlled over "machinery" to make such structures "other tangible property."[65] The court concluded that since

57. Treas. Reg. § 1.48-1(c) (1975).

58. 1969-1 CUM. BULL. 27.

59. The cable support towers are the towers located between the two terminal towers. The ruling did not deal with the proper classification of the terminal towers that support motors, gear assemblies, and lift controls.

60. 60 T. C. 861 (1973).

61. The court stated: "Even if the 'Astro-Needle' might be regarded as a type of 'machinery', to hold that such a formidable structure was not 'inherently permanent' would obliterate the distinction between 'personal property' and 'other tangible property'." *Id.* at 866.

62. 62 T.C. 446 (1974).

63. *See* note 58 *supra* and accompanying text.

64. The taxpayer strenuously argued that the property be characterized "tangible personal property" because the operation of a ski lift is not a "transportation" activity which would qualify "other tangible property" for the credit. Rev. Rul. 69-13, 1969-1 CUM. BULL. 25.

65. *See* note 61 *supra* and accompanying text.

the intervening support towers had no more inherent permanence than the terminal towers, and since the whole lift functioned as a unitary mechanism, *all* the towers must be tangible personal property, even though inherently permanent structures, because they constituted property in the nature of machinery.[66]

One hopes that the Commissioner's future position, in the interest of clarity, will be that which he expressed as the concession on the terminal towers in *Weirick*: inherently permanent structures in the nature of machinery are to be considered tangible personal property. Certainly this interpretation seems more consonant with the expressed congressional purpose of encouraging investment in equipment by broadly construing the reach of tangible personal property. Nevertheless, until there is a formal reaction from the Treasury to *Weirick*, the status of equipment which is both an inherently permanent structure and in the nature of machinery will remain unclear.

C. *Conclusion: Tangible Personal Property*

To recapitulate, it seems that the original congressional intent that tangible personal property be construed broadly, reinforced by an early ruling dealing with property used at a bank, has become somewhat overgrown by subsequent rulings intended to narrow the reach of this happiest (because immune from use restrictions) of property categories for taxpayers. Although the Committee Reports probably intended to broaden tangible personal property by freeing the concept from state fixture law, the regulations ominously note that a characterization of property as "personal" under state law is not controlling either, thus narrowing the concept. The Commissioner has further narrowed the tangible personal property category by quietly failing to recognize or assert the liberal "accessorial to the business" test for items found within a building. Nevertheless, items contained in or attached to a building remain the most comprehensive class of tangible personal property. The largest headache in the area is caused by confusion over the proper relationship between the statement in section 1.48-1(c) of the Regulations that "all property which is in the nature of machinery (other than structural components . . .)" is considered tangible personal property and the statement in the same section that " 'tangible personal property' means any tangible property except . . . inherently permanent structures." *Weirick* holds that the first-quoted passage controls over the second; *Roberts* holds the opposite. The briefs in *Weirick*

66. 62 T.C. at 451.

indicate that the Commissioner is as confused as everyone else over the proper resolution of this issue.

IV. Other Tangible Property

A. *Legislative History and Regulations*

"Other tangible property" is basically all real property except buildings and their structural components.[67] Whereas tangible personal property will generally qualify for the investment credit regardless of the nature of the taxpayer's activity,[68] "other tangible property" must be used as an "integral part" of "manufacturing, production, or extraction" or of "furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services"; or the property must qualify as a "research facility" or "facility for the bulk storage of fungible commodities" used "in connection with" any of the aforementioned activities. The regulations distinguish between property used as an integral part of "manufacturing, production, or extraction" and that used as part of "furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services" by appending to the latter category the requirement that the user of the property be engaged in the trade or business of furnishing these services.[69]

The Committee Report lists blast furnaces, railroad tracks and signals, oil and gas pipelines, and fences as examples of "other tangible property,"[70] importing the common-law notion that items affixed to the land should be considered realty, not personalty. The decision to give new life to this quaint archaism, coupled with the statement that "items of a mechanical nature" were to be considered personalty,[71] certainly does not simplify the identification of section 38 property.[72] Often, of course, there is no difficulty in determining whether an item is, or is not, personal property: a road, for example, clearly is not.[73] But as items on land physically rise above it and their metaphysical unity with the earth becomes more attenuated, problems arise.

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67. 1962 Report, supra note 3, at 415.

68. It will qualify for the investment unless it falls within one of the proscribed categories listed in §§ 48(a)(2)-(9). *See* note 13 *supra*.

69. Treas. Reg. § 1.48-1(d)(1) (1975).

70. 1962 Report, *supra* note 3, at 416.

71. *See* note 27 *supra* and accompanying text.

72. One may wonder why the signal apparatus at a railroad crossing is not an item of "mechanical nature." A clean break with the common-law past might have been preferable.

73. A roadway used solely by trucks in transporting raw materials for the taxpayer's business can qualify for the credit, but roadways designed for general use cannot. Rev. Rul. 71-555, 1971-2 Cum. Bull. 65.

B. *Distinguishing "Other Tangible Property" from "Tangible Personal Property"*

(1) Improvements to Land

The earliest test to be elucidated for distinguishing between tangible personal property and other tangible property was the "improvement to land" test. Revenue Ruling 65-308[74] labeled gas mains "other tangible property" since they were "improvements added to land in the form of inherently permanent structures which are placed in or upon land."[75] The Ruling did not expound on the concept of "inherently permanent structure," but the result reached seems plainly in accord with the expressed intention of the Committee Reports, as are the conclusions that steam mains,[76] water wells,[77] paved barnyards,[78] and tiled drainage ditches[79] also constitute "other tangible property."

The Service applied the same approach in Revenue Ruling 69-273,[80] concluding that the underground pipe and valve network of a golf course sprinkling system must be "other tangible property." While the analogy between water pipes and steam pipes is apparent, it must be noted that the sprinklers themselves, as well as the pumps, were classified as qualifying tangible personal property. It would seem equally reasonable to have treated the entire sprinkling system as a unitary mechanism; it seems somewhat simplistic to conclude that merely because an item is buried it must be considered an improvement to land as an inherently permanent structure. Nevertheless, it remains the Service's position that subterranean items are usually inherently permanent structures,[81] and this proposition generally has been sustained by the courts.[82]

An example of improvements to the surface of the land is the earthen boarding ramp of a ski lift.[83] The category of improvements to land as a standard for determining what is the other tangible property also includes "improvements to water." For example,

74. 1965-2 CUM. BULL. 74. This ruling dealt with a § 179 problem, but applied the principles developed under the investment credit.

75. *Id.*

76. Rev. Rul. 68-184, 1968-1 CUM. BULL. 7, 8.

77. Rev. Rul. 66-89, 1966-1 CUM. BULL. 7, 8.

78. *Id.*

79. *Id.*

80. 1969-1 CUM. BULL. 30. *See* note 53 *supra* and accompanying text.

81. *See, e.g.*, Rev. Rul. 74-152, 1974 INT. REV. BULL. No. 14, at 8 (underground storage tanks for gasoline).

82. *E.g.*, Tejas Properties, Inc. v. United States, 70-1 U.S. Tax Cas. ¶ 9240 (E.D. Tex. 1970); C.C. Everhart, 61 T.C. 328, 331 (1973).

83. Joseph B. Weirick, 62 T.C. 446 (1974).

docks,[84] permanent pilings,[85] piers,[86] mooring cells,[87] a lobster pound extending into an inlet,[88] dams,[89] and various pools, fish ladders, and other paraphenalia for keeping fish from being minced in the turbines at a hydroelectric dam[90] have all been classed as improvements to land.

(2) "Inherently Permanent Structures": The Three Tests

Property which constitutes "improvements to land" is not the only category of other tangible property. An "inherently permanent structure," whether or not an obvious improvement to land, is also other tangible property. An obvious example of an "inherently permanent structure" is a building; however, buildings never qualify for the credit, if they are "buildings" within the statutory sense.[91] What, then, is an "inherently permanent (non-'building') structure"? One test often invoked by the Service to answer this question might be called the "annexation" test. Under this test, the Service takes the position that a solidly constructed structure, although movable, is "other tangible property" because attached, and therefore annexed, to the realty. In many cases, the results seem sound. For example, in Revenue Ruling 68-62[92] billboards were held to be realty because of their size and secure affixation to the ground. Although one may incline to skepticism concerning the continued utility of the common law of structures as realty, the result in that ruling does no violence to the policy of the investment credit.[93]

Similarly, the Service classified the line towers of a chair lift as inherently permanent structures because of their sturdy construction.[94] The reasoning expressed in Revenue Ruling 68-345,[95] however, is less compelling. The Commissioner there ruled that metal canopies erected over the pump islands at filling stations,

84. Rev. Rul. 67-67, 1967-1 CUM. BULL. 6 (dictum).

85. Estate of Shirley Morgan, 52 T.C. 478, 483 (1969), *aff'd*, 448 F.2d 1397 (9th Cir. 1971) (per curiam).

86. Rev. Rul. 68-280, 1968-1 CUM. BULL. 20.

87. Rev. Rul. 68-211, 1968-1 CUM. BULL. 17.

88. Rev. Rul. 68-279, 1968-1 CUM. BULL. 18.

89. Rev. Rul. 73-420, 1973-2 CUM. BULL. 9.

90. Rev. Rul. 73-466, 1973-2 CUM. BULL. 52.

91. The statute specifically excludes buildings and their structural components in § 48(a)(1)(B). *See* text accompanying note 9 *supra*.

92. 1968-1 CUM. BULL. 365. This was a § 1245 issue, but investment credit principles were applied.

93. It is difficult to discern precisely what connection there might be between fostering the effacement of the landscape through billboards and expanding this country's capital expenditures to enable our goods to compete successfully overseas.

94. Rev. Rul. 69-169, 1969-1 CUM. BULL. 277. See, however, the discussion in the text following note 62 *supra*.

95. 1968-2 CUM. BULL. 30.

though designed for simple removal, were ineligible[96] "other tangible property." Despite the ease of disassembly, the Ruling nevertheless maintained that the canopies' function *while erected* was that of a permanent structure providing shelter, thus removing them from the category of personal property. Even less convincing than that ruling are some of the conclusions expressed in Revenue Ruling 69-170,[97] dealing with various components of a modern baseball stadium. The Service allowed the credit for flagpoles, backstops, and various lighted signs (not including the field lights) affixed to the stadium itself as tangible personal property,[98] but refused to allow it for flagpoles, screens, and electric signs attached to the *ground*; the Ruling's reasoning was that these free-standing components must be nonqualifying inherently permanent structures, simply because they were attached to the earth rather than to a building.[99] This seems to be a distinction without a difference. One wonders whether, following this approach, a giant amusement slide ruled ineligible for the credit as an inherently permanent structure[100] might have qualified as tangible personal property had it been erected inside, and therefore attached to, some building such as a fun house.

The conclusion in the baseball stadium Ruling was in itself a departure from and inconsistent with a previous statement in Revenue Ruling 67-23[101] that the matter of annexation to the ground or attachment to a building was not a controlling factor. That 1967 Ruling had held that an outdoor lighting facility was an inherently permanent structure, not tangible personal property, despite the fact that the facility was both easily removable and attached to a building. As noted earlier, the Service disallowed the credit for the field lights in the baseball Ruling, even though they were affixed to the stadium structure; apparently the Service believed that consistency of result was more important than consistency of reasoning. Reading the two Rulings together, one must reach the logically unsatisfactory conclusion that while attachment to a building rather than the ground may save an item from classification as other tangible property because an inherently permanent structure, sometimes

96. The canopies were ineligible for the credit because the retail sale of gasoline does not fall within "manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services," and therefore the use requirements for "other tangible property" were not complied with. INT. REV. CODE OF 1954, § 48(a)(1)(B).

97. 1969-1 CUM. BULL. 28.

98. *See* note 45 *supra* and accompanying text.

99. 1969-1 CUM. BULL. 28, 29.

100. Rev. Rul. 71-377, 1971-2 CUM. BULL. 63.

101. 1967-1 CUM. BULL. 5,6.

it will not; further, outdoor lighting facilities, no matter where attached, can never be personal property. Perhaps wisely, the Commissioner has not recently referred to either of these Rulings.

The Tax Court, attempting to inject some consistency into the inherently permanent structure confusion, observed in *Roberts*[102] that the controlling factor should not be whether the item in question was affixed to the land, but the *manner* and *permanence* of the arrangement.[103] Thus, the concrete base supporting an observation tower was declared an inherently permanent structure, since it was sunk into the soil and was unlikely to be moved without great effort. The same approach was borrowed for use in a section 179 problem in *Kenneth D. La Croix*,[104] which held that citrus trees were not tangible personal property because of their permanence.[105]

The Tax Court has also made clear, to the Commissioner's chagrin, that the inquiry into the nature and permanence of annexation works both ways. In *Estate of Shirley Morgan*,[106] the Commissioner took the position that a series of floating docks[107] were inherently permanent structures because of their attachment to the realty. Specifically, he pointed out that the docks were annexed to the land by the pilings anchoring them in place, by the gangway connecting the dock to the shoreline, and by plumbing and electrical power hookups.[108] The court dismissed the argument that a finding of technical annexation ended the inquiry, choosing instead to examine the significance of the attachment. Noting that the docks were easily removed from the pilings, that the gangways were merely rolled onto the docks, and that the plumbing and electrical lines were easily disconnected, the court concluded that the requisite permanence was lacking, and that the docks were indeed personal property.[109]

In *Joseph H. Moore*,[110] the Service argued that mobile homes

102. 60 T.C. at 861. *See also* text accompanying note 47 *supra*.

103. 60 T.C. at 866.

104. 61 T.C. 471, 487 (1974).

105. As in *Roberts*, however, the *La Croix* court observed that the mere fact of annexation to the realty did not, without more, prevent an object from being considered tangible personal property.

106. 52 T.C. 478, 483-84 (1969).

107. The walkways of the docks were kept in position by wooden pilings passing through openings in the walkways and sunk into the floor of the estuary; the walkways floated up and down with the nine foot tides, and could easily be moved to another location if desired.

108. The Service also advanced the argument that the docks should be considered "inherently permanent structures" because of their use. *See* note 114 *infra* and accompanying text.

109. By contrast, the court concluded that the pilings did exhibit the requisite degree of permanence.

110. 58 T.C. 1045 (1972), *aff'd*, 74-1 U.S. Tax Cas. ¶ 9146 (5th Cir. 1973) (per curiam).

in a trailer park were rendered inherently permanent structures by their attachment to the realty through utility connections. The Tax Court held otherwise, concluding that this trivial attachment was outweighed by the ease with which a mobile home could be transported from place to place, preventing it from becoming a "permanent" structure. Similar conclusions have been reached with regard to a transportable sewage processing plant[111] and movable wooden boarding ramps at a chair lift.[112] In short, the Commissioner has been quite unsuccessful in his attempts to convince the courts that the simple fact of attachment compels the "inherently permanent" conclusion; instead, an object which is intended to be moved, or which *could* be moved without undue effort may well be labeled personal property by the courts.

The Commissioner has also sought to employ a "functional" test to find that an item is an inherently permanent structure and thus other tangible property for investment credit purposes. Although this approach has had considerable success on other issues concerning the section 38 property controversy (most notably on the issue of whether an item is a "building" or a "structural component")[113] it has been met with judicial skepticism in this area. Basically, the Commissioner's argument has been that if the property in question is used in the same manner as or in place of a more familiar object which is concededly permanent, then the property under consideration must also be deemed an inherently permanent structure. In Revenue Ruling 67-67[114] and in *Estate of Shirley Morgan*[115] the Commissioner contended that since the floating docks were employed in place of similar nonfloating (and therefore obviously permanent) berthing facilities, this *use* should result in "inherently permanent" treatment for *floating* docks.[116] Rejecting the proffered analogy, the Tax Court held that the permanence of a particular item was to be evaluated with reference to that item's own intrinsic nature, and that similarity of function could not be employed to impose a sort of constructive permanence on an item which was essentially impermanent. This is an eminently sensible resolution.

111. *See* note 55 *supra* and accompanying text.
112. Joseph B. Weirick, 62 T.C. 446, 449 (1974).
113. *See* text following notes 233 & 308, *infra*.
114. 1967-1 CUM. BULL. 6.
115. 52 T.C. 478, 483 (1969).
116. Similarly, in Rev. Rul. 67-156, 1967-1 CUM. BULL. 7, and in Joseph H. Moore, 58 T.C. 1045 (1972), the Service took the position that the use of a motor vehicle trailer as a laundrette or home in place of and in the same manner as a more permanent structure required the trailers to be treated as buildings.

(3) Property of an "Inherently Permanent Nature"

One final formulation for other tangible property is property of an "inherently permanent nature." Like "inherently permanent structure," the term is vague; but unlike "inherently permanent structure," it does not appear in the regulations, nor is it amplified by any substantial body of rulings and decisions. Instead, it appears to be a stopgap term reserved for situations not fitting any of the other, better defined, formulations. It was applied in Revenue Ruling 70-103,[117] to characterize walls, doors, restrooms, plumbing, office partitions, flooring, and electrical fixtures added and employed by the taxpayer to convert a worked-out limestone mine to a warehousing area. Normally, such items would fall into the category of "structural components of buildings or other inherently permanent structures,"[118] but here the Service apparently was not willing to label an old mine as a "building" or a "structure." Equally reluctant, however, to let these items escape as tangible personal property, the Service coined the term "items of an inherently permanent nature" to conclude that they were other tangible property. The result in the Ruling seems correct, but one wonders if the Service will be able to resist the temptation to expand this presently vague rubric into yet another test for removing property from the personal classification and thus denying the credit.

C. *Determining What "Other Tangible Property" Qualifies for the Credit*

(1) Elements of the "Integral Part" Test

Assuming that an item has been classified as "other tangible property" for whatever reason, it yet may qualify for the credit if it is used "as an integral part" of certain specified activities. The original Committee Reports do not define the meaning of "integral part," although they do mention "blast furnaces, oil and gas pipelines, railroad track and signals, and fences used in connection with raising of cattle" as examples of qualifying items.[119] The regulations clarify the matter somewhat, stating that:

> Property is used as an integral part of one of the specified activities if it is used directly in the activity and is essential to the completeness of the

117. 1970-1 CUM. BULL. 6.

118. *See generally* text following note 308 *infra*.

119. 1962 REPORT, *supra* note 3, at 416. The use of the term "in connection with" in describing qualifying fences was probably inadvertent, since fences are subject to the more stringent "integral part" test. The error was corrected in the Technical Explanations, which made clear that these fences should be used "as an integral part" of an activity. 1962 TECH. EXPLANATION, *supra* note 10, at 517.

> activity. Thus, for example, in determining whether property is used as an integral part of manufacturing, all properties used by the taxpayer in acquiring or transporting raw materials or supplies to the point where the actual processing commences (such as docks, railroad tracks and bridges), or in processing raw materials into the taxpayer's final product, would be considered as property used as an integral part of manufacturing.[120]

Generally, the Service has been reasonably liberal in applying its "used directly in, and essential to the completeness of" test on the question of "integral part." For example, the storage tanks, loading and unloading docks, various racks and pumps for filling trucks, and the paved yard of an oil blending facility were all held to be integral parts of the blending process.[121] In other rulings, the Service has allowed the credit for a mooring cell used by a barge company to provide a temporary anchorage point,[122] safety devices such as concrete firewalls constructed around gasoline storage tanks at a refinery,[123] wells (whether lined or not) and drainage facilities constructed on a farm,[124] test tracks constructed by an automobile manufacturer for evaluating new prototypes,[125] and paved areas at an airport for parking aircraft.[126] The Service, reversing an earlier hostility toward allowing the credit for such expenditures,[127] has even permitted the credit for land preparation costs, if so closely associated with other qualifying assets that they must be replaced contemporaneously with those assets.[128]

Assets such as blast furnaces would always seem to meet the integral part test, but other types of property, such as roads and parking areas, require more careful examination. Here, the Service interprets the integral part test to require employment of facilities predominantly by vehicles actually engaged in the qualifying activity. Thus, roadways and parking areas within a manufacturing complex used solely, or regularly, by trucks transporting raw materials qualify;[129] however, similar facilities used predominantly as parking facilities for employee and visitor convenience do not qualify, even

120. Treas. Reg. § 1.48-1(d)(4) (1975). The regulations add telephone poles, broadcasting towers, and oil derricks to the list of qualifying property given in the original Committee Reports. *Id.*

121. Rev. Rul. 74-204, 1974 INT. REV. BULL. No. 18, at 7.

122. Rev. Rul 68-211, 1968-1 CUM. BULL. 17. The loading and unloading activities did not take place at these mooring cells, but the Service was not disposed to make difficulties because of this.

123. Rev. Rul. 68-347, 1968-2 CUM. BULL. 33.

124. Rev. Rul. 72-272, 1972-1 CUM. BULL. 17; Rev. Rul. 66-89, 1966-1 CUM. BULL. 7.

125. Rev. Rul. 72-267, 1972-1 CUM. BULL. 18,19.

126. Rev. Rul. 69-329, 1969-1 CUM. BULL. 30.

127. The Commissioner had unsuccessfully taken a more hostile position in Norfolk Shipbuilding & Drydock Corp. v. United States, 321 F. Supp. 222 (E.D. Va. 1971).

128. Rev. Rul. 72-96, 1972-1 CUM. BULL. 67.

129. Rev. Rul. 71-555, 1971-2 CUM. BULL. 65.

though used in the operation of the business, because of insufficient nexus with the manufacturing, production, or extraction.[130] Fences are another category of property whose qualification as an integral part is subject to a somewhat stricter burden of persuasion. Fences employed in agricultural activities to control the movement of livestock will qualify,[131] as will guardrails serving an analogous function in the containment of vehicular traffic at a marshalling yard.[132] The Service finds a distinction, however, between fences thus employed and those erected merely as barriers to unauthorized entry, classifying the latter as "incidental."[133] Outdoor lighting facilities are another special case, and will qualify only on proof of substantial nocturnal activity necessitating artificial lighting.

It should be noted that the Service takes the position that "used directly in, and essential to, the completeness of" an activity is to be interpreted in terms of systemic integration; that is, if an item is to be an integral part of a process, it must be because the mechanics of the process itself, rather than external factors, require its inclusion. Thus Revenue Ruling 73-466[134] concluded that certain fish preservation facilities constructed at a hydroelectric plant pursuant to Federal Power Commission order[135] were not used as an integral part of furnishing energy, even though the taxpayer had no choice but to comply with the agency order and therefore could not have operated the hydroelectric facility without the fish ladders. On the other hand, it would seem that some sort of system intended to prevent fish from entering and damaging the turbines would have qualified as an integral part of furnishing electric power, being necessary for the proper functioning of the generating system.

Although there was controversy in the area for some time, the reach of "manufacturing, production, or extraction" is now an even quieter front than the "integral part" issue. The Committee Reports made no effort to define those terms, but the Technical Explanations indicate that the terms are to be given their commonly ac-

130. Rev. Rul. 72-397, 1972-2 CUM. BULL. 8; *see* note 123 *supra* and accompanying text. Similarly, fire prevention measures may not always qualify: as noted earlier, firewalls at a refinery were approved, but fire hydrants emplaced at a marine terminal were disqualified in a questionable ruling dismissing them as "general land improvements" not sufficiently related to the terminal's activity. Rev. Rul. 68-280, 1968-1 CUM. BULL. 20. It is true that the terminal probably could function without its fire hydrants, but to define "integral part" so narrowly that it is tantamount to "sine qua non" seems altogether too niggardly.

131. Rev. Rul. 66-89, 1966-1 CUM. BULL. 7.

132. Rev. Rul. 68-280, 1968-1 CUM. BULL. 20.

133. *Id.* at 21; Rev. Rul. 68-1, 1968-1 CUM. BULL. 8.

134. 1973-2 CUM. BULL. 52.

135. The facilities involved consisted of an entrance pool, a fish ladder, a holding pool, a mechanism for lifting fish from the holding pool into trucks, water pipes, and a collection pool.

cepted meanings. Further, the Explanations include within "manufacturing and production" all activities involving the construction, reconstruction, or making of property

> from or with scrap, salvage, or junk material, as well as from new or raw material, (1) by processing, manipulating, refining, or changing the form of an article, or (2) by combining or assembling two or more articles, and includes the cultivation of the soil and the raising of livestock and other farm produce.[136]

The regulations repeat the quoted language and set forth an extensive list of activities illustrating the scope of "manufacturing, production, or extraction."[137] The Service's position is quite liberal. At one point the Commissioner did take the position that the blending of two different grades of oil to produce a third was a "service" not comprehended by manufacturing or production, but discovered in *Northville Dock Corp.*[138] that the Tax Court was prepared to interpret these terms more liberally. The court concluded that the blending fell within "the making of property by changing the form of an article, or by combining or assembling two or more articles."[139] The Commissioner later accepted this interpretation in Revenue Ruling 74-204.[140]

The Technical Explanations to the 1962 Revenue Act indicate that "transportation," "communications," "electrical energy," "gas," "water," or "sewage disposal" are also to be given their commonly accepted meanings in determining whether a taxpayer's operations fall within them.[141] Unlike manufacturing, production, or extraction, however, the Explanations provide that property will not be considered employed as an integral part of one of these service activities unless the property is used by one engaged in the trade or business of furnishing such services.[142] This additional requirement is found also in the regulations, although it did not appear in so

136. 1962 TECH. EXPLANATION, *supra* note 10, at 516. The TECH. EXPLANATION lists as examples of such activities: "extraction, processing, refining, and fabrication of minerals or mineral products; the growing, raising, processing, and packing or packaging of foodstuffs; the operation of sawmills and the production of lumber and lumber products and other building materials, and the manufacture, treatment, and packaging of textiles, paper, leather goods, glass, etc." *Id.* at 516-17.

137. The list in the regulations includes: "the extracting, processing, or refining of metallic and nonmetallic minerals, including oil, gas, rock, marble, or slate; the construction of roads, bridges, or housing; the processing of meat, fish, or other foodstuffs; the cultivation of orchards, gardens, or nurseries; the operation of sawmills, the production of lumber, lumber products, or other building materials; the fabrication or treatment of textiles, paper, leather goods, or glass; and the rebuilding, as distinguished from the mere repairing, of machinery." Treas. Reg. § 1.48-1(d)(2) (1964).

138. 52 T.C. 68 (1969), *aff'd* 427 F.2d 164 (2d Cir. 1970) (per curiam).

139. *Id.* at 73 (quoting Treas. Reg. § 1.48-1(d)(2) (1964)).

140. 1974 INT. REV. BULL. No. 18, at 7.

141. 1962 TECH. EXPLANATION, *supra* note 10, at 516.

142. *Id.* at 517.

many words in either the body of the Committee Reports or in section 48 itself.[143] The Technical Explanations use railroads and airlines as illustrations of the transportation business, and telephone, telegraph, or radio or television broadcasting as examples of the communications business.[144] The regulations supply bus lines, shipping and trucking companies, and oil pipeline companies as further examples.[145] As with manufacturing and production, the Service is ordinarily cooperative on just what activities fall within the ambit of transportation, etc., but it has refused to accede to some of the more imaginative arguments advanced by taxpayers; thus neither the Service[146] nor the Tax Court[147] considers the operation of a ski lift as the furnishing of transportation.

The Service may be less cooperative on the issue of whether the taxpayer is engaged in the trade or business of furnishing electricity, water, or similar services, preferring that such activities be the taxpayer's *primary* trade or business in order to qualify. In Revenue Ruling 67-433,[148] the owner-lessor of a shopping center metered and billed its tenants for their use of water and electricity. Nevertheless, the Service concluded that because the taxpayer's *primary* trade or business was the furnishing of space to its tenants, its activities as a conduit for utility services must be merely incidental, despite the existence of a profit on those services. Therefore, the taxpayer's boilers, pumps, tanks, meters, and other water treatment and electrical equipment could not qualify for the credit, since the owner-lessor was not in the trade or business of furnishing electrical energy or water services "as contemplated by the regulations."[149]

Although this "primary trade or business" interpretation seems restrictive, thus far it has survived judicial scrutiny. The Tax Court

143. Treas. Reg. § 1.48-1(d)(1) (1964). The requirement did not appear in either section 48 itself or the body of the Committee Reports. As earlier noted, it is doubtless drawn from the reference in § 46(c)(3)(B) concerning "public utility property," to "property used predominantly in the trade or business of furnishing" the utility activities. The regulations' position is not unreasonable, since § 48(a)(1)(B)(i) does read: "manufacturing, production, or extraction, *or of* furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services." [Emphasis supplied]. The use of the italicized "or of" seems to indicate some distinction between the two groups of activities, lending plausibility to the Service's position. This position has been sustained by the Tax Court in Mount Mansfield Co., 50 T.C. 798 (1968) and Frank J. Evans, 48 T.C. 704 (1967), *aff'd*, 413 F.2d 1047 (9th Cir. 1969) (per curiam).

144. 1962 TECH. EXPLANATION, *supra* note 10, at 517.

145. Treas. Reg. § 1.48-1(d)(3) (1964).

146. Rev. Rul. 69-13, 1969-1 CUM. BULL. 25.

147. Mount Mansfield Co., 50 T.C. 798 (1968).

148. 1967-2 CUM. BULL. 51.

149. *Id.* at 53. *See also* Rev. Rul. 69-273, 1969-1 CUM. BULL. 30 (since a golf course is not in the trade or business of furnishing water, underground components of sprinkler system do not qualify for credit).

held in *Frank J. Evans*[150] that the furnishing of electricity, water, gas, and sewage services by the operator of a trailer court to his tenants did not constitute a distinct trade or business, indicating that a showing of significant time spent repairing, maintaining, or supervising the systems, as well as more careful records showing some substantial amount of gross receipts, net profit, or even a good faith anticipation of a profit might have buttressed the taxpayer's case.[151]

Similarly, in *Tejas Properties, Inc. v. United States*[152] a developer of residential properties was not allowed the credit for a water storage tank and sewage disposal system installed to encourage the sale of lots, for lack of the proper trade or business. The court specifically adverted to the taxpayer's irregular billing procedures, his failure to allocate costs to the services on his books, and the apparent absence of intent to derive a profit from the services in question. *Hayden Island*[153] denied the credit for certain water and sewer lines constructed by a developer who had "no thought" of making a profit from these activities.

Some intent to show a profit, then, is crucial; and though neither *Tejas Properties* nor *Hayden Island* expressly imposed the "primary trade or business" requirement, their findings of lack of a trade or business are not inconsistent with that requirement. Consequently, to have any chance at all at the credit for equipment used to furnish electricity, water or similar services, the taxpayer must document his utility activities as a separate, profit-making operation; even then the credit may be disallowed if a court agrees with the Service, as in *Evans*, that this activity must be the taxpayer's primary trade or business.

(2) Research and Storage Facilities: A Special Situation

Even if other tangible property is not used as an "integral part" of manufacturing, production, extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, it may still qualify for the credit if it serves as a "research facility" or as a "facility for the bulk storage of fungible commodities (including commodities in a liquid or gaseous state),"

150. 48 T.C. 704 (1967).

151. *Id.* at 708. Judge Tannenwald, concurring, felt such an inquiry unnecessary, unduly burdensome, and at variance with his interpretation of the statute, which would limit the credit to *suppliers* (such as power stations) of these services, excluding conduits or consumers, as he conceived the taxpayer in this case to be. *Id.* at 710.

152. 70-1 U.S. Tax Cas. ¶ 9240 (E.D. Tex. 1970).

153. 74-2 U.S. Tax Cas. ¶ 9604 (D. Ore. 1974).

"in connection with" any of those activities.[154] "In connection with" connotes a lesser nexus with the qualifying activity than does "integral part."[155]

Neither the Committee Reports nor the Technical Explanations define or illustrate the term "research facilities." The regulations also avoid defining the term, but they do cite wind tunnels and test stands as examples.[156] "Facilities for the bulk storage of fungible commodities" are more clearly defined, and have become encrusted with a sizeable body of rulings and judicial decisions. The original enactment referred simply to "storage facilities."[157] The 1971 amendments, however, perhaps in an attempt to narrow the development of the concept,[158] substituted the current wording with its emphasis on "bulk" and "fungible", and the continued viability of the considerable body of pre-1971 rulings and decisions is somewhat unclear.[159]

There is a surface contradiction between the statute's allowance of the credit for storage facilities and its simultaneous disqualification of buildings. Significantly, the Technical Explanations provide that "warehouses" are to be considered nonqualifying "buildings."[160] Some peculiar characteristics must distinguish storage facilities (as they were termed before 1971) from warehouses and other buildings.

Because the statute singles out storage facilities for special treatment by virtue of their *use*, the Service early decided that function must be the key distinction. In Revenue Ruling 66-89,[161] the Service approved the credit for such items of farm property as corn cribs, grain storage bins, and silos, but denied it for barns, stables, poultry houses, and warehouses. In the Service's opinion, a two-pronged function test had to be met: the facility must be presently used for storage, and must not be reasonably adaptable for other uses. Barns and the other examples of nonqualifying property failed the second prong of the test because they provided working space,

154. INT. REV. CODE OF 1954, §§ 48(a)(1)(B)(ii), (iii).

155. The 1962 Technical Explanations state: "Research or storage facilities (other than buildings) are eligible for the credit if used in connection with any of the specified activities, although such property is not an integral part of the activity." 1962 TECH. EXPLANATION, *supra* note 10, at 517.

156. Treas. Reg. § 1.48-1(d)(5)(i) (1964).

157. Act of Oct. 16, 1962, Pub. L. No. 87-834, 76 Stat. 960.

158. *See* Kraus, *New Developments in the Investment Tax Credit*, 20 TUL. TAX INST. 237 (1971).

159. *See* Merchants Refrigerating Co., 60 T.C. 856, 859-60 (1973).

160. 1962 TECH. EXPLANATION, *supra* note 10, at 516. The difference is based on a difference in the activity conducted. Rev. Rul. 74-451, 1974 INT. REV. BULL. No. 38, at 7.

161. 1966-1 CUM. BULL. 7.

wherein the farmer was carrying on other activities besides simply storage.

Certain limited activities "incidental to storage" do not result in disqualification, however: for example, it was held permissible for the owner of a potato storage facility to operate vents to dissipate heat generated by the stored potatoes and to push the potatoes into a central transportation canal for movement to another building.[162] The Service specifically noted that the cleaning, processing, and grading of the potatoes was conducted elsewhere, indicating that these would be disqualifying activities if done within the storage facility.[163]

The Commissioner's view of the scope of permissible activities within a storage facility was first challenged in *Robert E. Catron*,[164] in a dispute over the proper classification of a quonset hut-like structure. One third of this structure was used by its farmer-owner for the cold-storage of boxed apples; this heavily insulated storage area was set off from the rest of the structure by a floor-to-ceiling partition pierced by a refrigerator door. The taxpayer conceded that sorting and processing took place in the uninsulated area, but argued that this did not in any way detract from the status of the insulated area as a storage facility, in which the only work performed was the insertion or removal of the stored commodity. The Commissioner retorted that a building was a building, and that no allocation was possible for parts of a building assertedly used for storage: in his opinion the processing carried out in the uninsulated two-thirds disqualified the entire structure. The Tax Court first approved the concept of a functional inquiry for distinguishing the special class of storage facilities from ordinary "buildings," and observed that the nonrefrigerated two-thirds of the quonset hut where the apples were sorted and otherwise processed was a nonqualifying "building," not a storage facility, because it provided working space.[165] The court rejected the Commissioner's "all-or-nothing" argument,[166] however, observing that an allocation could

162. Rev. Rul. 68-132, 1968-1 CUM. BULL. 10, 14, *modified*, Rev. Rul. 71-359, 1971-2 CUM. BULL. 61, 63 (excising references to the "predominant use" test).

163. *Id.* In addition to the emphasis on the activities conducted within the facility, another common thread appearing in the pre-1971 rulings was that all the commodities stored within approved facilities were fungible in nature. Thus, storage facilities approved included those used for fungibles such as grain, Rev. Rul. 68-297, 1968-1 CUM. BULL. 27; potatoes, Rev. Rul. 68-132, 1968-1 CUM. BULL. 10; or coal, Rev. Rul. 66-89, 1966-1 CUM. BULL. 7. The Service did not avail itself of any opportunities to expand the concept in published rulings to packaged or otherwise sorted commodities.

164. 50 T.C. 306 (1968), *acquiesced in*, Rev. Rul. 72-365, 1972-2 CUM. BULL. 8.

165. This has often been cited as a key attribute of a "building." *See* text following note 243 *infra*.

166. The Commissioner had sought to justify this approach with the rather specious

and should be made if part of a structure did indeed function as a storage facility.[167] The court concluded that there was nothing to indicate that the storage of boxed apples[168] was not within the contemplation of the statute, and that the room qualified as a storage facility because Revenue Ruling 66-89's[169] two-pronged test had been met: the room was used only as a storage facility (the bringing in and removal of apples being only "incidental" activities), and was not reasonably adaptable to other uses because "the chilly temperatures which undoubtedly prevailed would surely limit its adaptability."[170]

Subsequent cases were substantially in accord with *Catron's* interpretation of the function test. Barley receiving stations for a brewery, in which barley might be stored for up to two years against possible crop failure, were approved because storage was the "main purpose" of the stations.[171] Moreover, certain incidental activities could be carried on within a storage facility and would not automatically disqualify it: thus, inhibition of the ripening of stored fruit in "sweet rooms" by various controlled temperature and humidity changes was permitted in *Central Citrus Co.*[172] over the Commissioner's objection that this processing destroyed the character of the areas as storage facilities. Similarly, the "not reasonably adaptable" prong of the function test was generally construed, as in *Catron*, to mean essentially "as currently operated not reasonably adaptable to other uses."[173] Thus, the barley-receiving stations mentioned above were held not reasonably adaptable to other uses simply because they had been designed for barley storage.[174] In the same vein, "the unusual dimensions and the varied extremes of tempera-

argument that taxpayers would throw the Treasury into chaos by claiming the credit for such things as broom closets under the "storage facility" rubric. The Tax Court accorded this argument the respect it deserved, noting that the Treasury had no difficulty allocating between buildings and fixtures or between business and personal use of property, and rejected the argument as founded on nought but administrative convenience. 50 T.C. at 314.

167. The Tax Court observed: "Conceptually and in practice it is not impossible to segregate a qualifying silo or grain-storage bin from a nonqualifying barn to which it may be attached . . . ." *Id.*

168. *But see* Treas. Reg. § 1.48-1(d)(5)(ii) (storage of boxed oranges does not qualify after the 1971 statutory amendments because it is not bulk storage of a fungible commodity), T.D. 7203, 1972-2 CUM. BULL. 12.

169. *See* note 161 *supra* and accompanying text.

170. 50 T.C. at 315.

171. Adolph Coors Co., 27 CCH Tax Ct. Mem. 1351, 1362 (1968).

172. 58 T.C. 365 (1972).

173. One must assume, after all, that the taxpayer there could have circumvented the "chilling effect" of the temperature on other activities in that room by merely shutting off the refrigeration equipment.

174. "The stations have no purpose except those stated herein and were designed and constructed to best accomplish those purposes and no others." 27 CCH Tax Ct. Mem. at 1362.

ture, humidity, and air content undoubtedly limited the [sweet] rooms' *reasonable* adaptability."[175]

One problem with the *Catron* line of cases is that they do not provide clear standards for the resolution of the "reasonable adaptability" issue. A confused district court, after complaining of *Catron's* imprecision, concluded in *Brown & Williamson Tobacco Corp. v. United States*[176] that certain tobacco storage sheds were not reasonably adaptable to other uses, although the Commissioner had introduced evidence demonstrating that eleven similar sheds had indeed been converted for other functions.[177]

An unsuccessful stratagem employed by the Commissioner to narrow the category of qualifying storage facilities was the "predominant use" test, which attempted to pare back the breadth of the "in connection with" requirement. Although the regulations conceded that the taxpayer-owner of a storage facility need not be engaged in the manufacturing process himself for the facility to satisfy the "in connection with" requirement,[178] the Service took the position in Revenue Rulings 67-220[179] and 68-122[180] that the predominant users of the facility must be directly engaged in the qualifying activity if the owner himself was not. Thus, a grain elevator used by its owner who bought, stored, and sold grain solely for his own account and in which no space was leased directly to farmers could not qualify.[181] The Commissioner had abysmal luck with this test in court. His first reverse came in *Schuyler Grain Co.*,[182] involving concrete grain storage bins owned and operated by a grain broker who rented no space to farmers, but who did process some 8% of the stored grain into animal feed and sold the balance. Although the

175. 58 T.C. at 371-72 (emphasis in original). Only occasionally was the Commissioner able to have this test tightened up somewhat as in *Palmer Olson*, 29 CCH Tax Ct. Mem. 1367 (1970), declaring that a quonset hut with moisture-proof floors, used for grain storage was disqualified because it had been used earlier to store farm implements. In that case, the court reversed the order of the elements of the test, observing that "[p]rincipally, the facility may not be reasonably adaptable to other uses, and secondly, it must provide only storage space and not working space." *Id.* at 1369. The court concluded that the quonset huts could not qualify, since they were "not unfit" for other use.

176. 369 F. Supp. 1283 (W.D. Ky. 1973), *aff'd*, 491 F.2d 1258 (6th Cir. 1974) (per curiam).

177. The court based its decision on the $1.60 per square foot cost of conversion (the buildings contained an average of 7700 square feet), and the nuisance involved in installing toilets, heat, sprinkler facilities, and the like.

178. Treas. Reg. § 1.48-1(d)(5) (1964).

179. 1967-2 CUM. BULL. 46, *revoked*, Rev. Rul. 71-359, 1971-2 CUM. BULL. 61.

180. 1968-1 CUM. BULL. 10, *revoked*, Rev. Rul. 71-359, 1971-2 CUM. BULL. 61.

181. *See also* Rev. Rul. 68-279, 1968-1 CUM. BULL. 18 (pound operated by lobster broker fails predominant use test; not revoked by 71-359); Rev. Rul. 68-282, 1968-1 CUM. BULL. 25 (peanut storage facility fails predominant use test; revoked by 71-359).

182. 50 T.C. 265 (1968), *aff'd*, 411 F.2d 649 (7th Cir. 1969), *acquiesced in*, Rev. Rul. 71-359, 1971-2 CUM. BULL. 61.

case did not turn on this issue, both the Tax Court and the Seventh Circuit evidenced considerable doubt about the validity of the predominant use test.[183] After *Schuyler Grain* the predominant use test suffered one judicial disaster after another,[184] and it finally was withdrawn in Revenue Ruling 71-359,[185] revoking several prior rulings.[186]

The predominant use test had hardly been accorded its overdue burial, however, when a new source of confusion was introduced into the law of storage facilities: the 1971 Revenue Act[187] changed the reference from "storage facilities" to a "facility used . . . for the bulk storage of fungible commodities (including commodities in a liquid or gaseous state)."[188] The Senate Finance Committee's Report indicated that while certain incidental activities could still be undertaken inside, "bulk storage" referred to the keeping of a commodity in a large mass prior to its consumption or utilization and that "fungible commodities" were those which were of such a nature that one part might be used in place of another.[189] The regulations were amended to reflect these changes; the regulations also contain an observation that the act of sorting and boxing the stored commodity destroys the requisite characteristic of storage in "bulk."[190]

In the recent case of *Merchants Refrigerating Co.*,[191] involving pre-1971 construction, the court followed *Catron* in allowing the credit for a free-standing cold storage room containing frozen foods

183. The Tax Court accused the Commissioner of trying "to impose a 'primary use' rule to section 38 property where none is provided for either in the statute or in the regulations." 50 T.C. at 270. The court continued: "However, we need not consider the merits of such an argument inasmuch as we conclude that the five bins in question were used 'in connection with' at least some of the activities enumerated in section 48." *Id.* The Court of Appeals noted that it could find no support for the predominant use test, were it applicable, in the regulations. 411 F.2d at 652.

184. *E.g.*, Sherley-Anderson-Rhea Elevator, Inc. v. United States, 315 F. Supp. 1055 (N.D. Tex. 1970); F.P. Wood & Son, Inc. v. United States, 314 F. Supp. 1205 (E.D.N.C. 1970); United States v. Loami Grain Co., 318 F. Supp. 349 (S.D. Ill. 1969).

185. 1971-2 CUM. BULL. 61 (revoking rulings 68-282, 68-122, and 67-220; modifying 68-132).

186. Even though the "predominant use" test no longer terrorizes the "in connection with" requirement, there must nevertheless be *some* nexus with a qualifying activity. *See, e.g.*, Rev. Rul. 74-152, 1974 INT. REV. BULL. No. 14, at 8 (storage facility used by seller of retail gasoline ineligible for the credit because of insufficient relation to qualifying activity).

187. Pub. L. No. 92-178, 85 Stat. 497 (codified in scattered sections of INT. REV. CODE OF 1954).

188. INT. REV. CODE OF 1954, § 48(a)(1)(B)(iii).

189. S. REP. No. 92-437, 92d Cong., 1st Sess. (1971) [Hereinafter cited as 1971 REPORT].

190. Treas. Reg. § 1.48-1(d)(5)(ii), T.D. 7203, 1972-2 CUM. BULL. 12. provides in pertinent part: "Bulk storage means the storage of a commodity in a large mass prior to its consumption or utilization. Thus, if a facility is used to store oranges that have been sorted and boxed, it is not used for bulk storage."

191. 60 T.C. 856 (1973).

packed in ready-to-market cartons. The court intimated, however, that in its opinion *Catron* and *Central Citrus* probably had been wrongly decided,[192] and noted with satisfaction that the statute they had interpreted was no longer in force.[193]

Recent examples of facilities certified by the Service as engaged in the bulk storage of fungible commodities include silos for unbagged cement,[194] underground tanks for gasoline,[195] and a refrigerated structure containing mostly unsorted apples brought directly in tote boxes from the orchard.[196] Despite the statement in the regulation that storage of boxed and sorted fruit will disqualify a structure, the Service has indicated that it will relent if the amount of such sorted articles comprises a relatively insignificant part of the total of items stored.[197] A structure used to freeze and store drums and cans of processed fruits, however, does not qualify.[198] Similarly, the Service feels that inventoried parts and individually identifiable assembly elements of articles in manufacture such as radios are not fungible, and cannot be considered stored in bulk.[199]

Notwithstanding the intimations in *Merchants Refrigerating*,[200] it may well be that the Commissioner's interpretation of "fungible" and "bulk" will be adjudged too narrow, should a taxpayer choose to litigate the issue. It is equally as reasonable to maintain that the intent of the 1971 amendment was merely to replace the extremely vague term "storage facility" (which *could* have been interpreted,

192. Accordingly, if the matter were one of first impression, there would be much force to the Government's position that Building F, plainly a type of warehouse, should, unlike a silo or gasoline storage tank, be regarded as a "building" within the meaning of the parenthetical language of clause (B) and that the freezer room within the structure should therefore fail to qualify as "section 38 property." But the course of decision has run in a different direction, and that result is precluded by at least two prior decisions of this Court holding that a storage facility may qualify for the investment credit even if it is a part of a larger structure having the physical attributes of a "building." (Citing *Catron* and *Central Citrus*).

Id. at 859-60.

193. The *Merchants* court felt that there was serious doubt of the continued validity of the propositions expressed in those cases that structures other than silos, storage tanks, and the like could qualify, or that the storage of boxed commodities was permissible. *Id.* at 860.

194. Rev. Rul. 72-365, 1972-2 CUM. BULL. 8.

195. Rev. Rul. 74-152, 1974 INT. REV. BULL. No. 14, at 8 (the nexus to a qualifying activity was missing, however, so the tanks were ineligible for the credit).

196. Rev. Rul. 74-451, 1974 INT. REV. BULL. No. 38, at 7.

197. *Id.*

198. Rev. Rul. 74-452, 1974 INT. REV. BULL. No. 38, at 8.

199. Rev. Rul. 74-3, 1974 INT. REV. BULL. No. 1, at 11.

200. *Merchants Refrigerating* was written by Judge Raum, whose view of section 38 property does not seem to be expansive. *See* Melvin Satrum, 62 T.C. 413, 419 (1974) (joining Dawson, J., dissenting); Beverly R. Roberts, 60 T.C. 861 (1973); Sunnyside Nurseries, 59 T.C. 113 (1972); Arne Thirup, 59 T.C. 122 (1972); Frank J. Evans, 48 T.C. 704, 710 (1967) (Tannenwald, J., concurring).

for example, to comprehend facilities used to garage tractors) with one that more clearly reflected the original intent of the 1962 enactment. Such an argument imparts continued validity to *Catron* and *Central Citrus*, and questions the correctness of the rulings which hold that tubs of processed food are not fungible containers of commodities stored in bulk. Further, the Senate Finance Committee indicated that fungible commodities are stored in bulk if kept in a mass prior to consumption or utilization;[201] a case certainly can be made for the proposition that food packed in numerous drums (each of which is essentially fungible) is still kept "in a mass," and that food which has been processed has nevertheless *not* yet been "consumed" or "utilized." A judicial adoption of this reasoning certainly would not mark the first instance of a court rejecting the Commissioner's overly narrow interpretation of a definitional element of section 38 property.

D. Conclusion: Other Tangible Property

Looking back from the Commissioner's restrictive interpretation of "bulk storage of fungible commodities" to the slippery concept of "inherently permanent structure" one observes that the landscape of "other tangible property" is cluttered with a confusing mass of concepts. "Inherently permanent structure" is not defined in the regulations, but the Commissioner apparently would like the term to include nearly everything buried under or attached to the land. He usually does not include items affixed to buildings, but one may be nearly certain that an outdoor lighting facility will be considered an inherently permanent structure, wherever affixed. The courts have quite properly refused in the main to accede to arguments advanced by the Service for the automatic classification as an inherently permanent structure of any structure attached in any manner to the realty, usually preferring to conduct at least a limited inquiry into the nature and permanence of attachment. Thus, the Commissioner's attempt to supply a metaphysical permanence to such impermanently rooted structures as floating docks by means of an unconvincing functional analogy have been rejected through a realization that intrinsic permanence and function are two distinct concepts, one of which cannot be supplied by the other. The Commissioner's truculence in this area stands in sharp contrast to his much more liberal approach to the meaning of "integral part," and "manufacturing, production or extraction." It is true that he

201. "Bulk storage has reference to the keeping of a commodity in a large mass prior to its consumption or utilization. The commodity must be fungible in nature; that is, of such a nature that one part may be used in place of another." 1971 REPORT, *supra* note 189 at 29.

prefers to view "integral part" in terms of internal systemic integration, thus excluding components of a system added in response to requirements imposed by such external sources as federal regulatory agencies—a narrow but not unreasonable view. The Commissioner's attitude on "manufacturing, production and extraction" has undoubtedly been influenced by the very unsympathetic judicial responses to his earlier, more restrictive interpretations. In a similar development, he has recanted his attempt to constrict the breadth of "in connection with" for storage and research facilities through the spectacularly unsuccessful "predominant use" test.

This change in attitude may be due partly to his contention that the 1971 amendments to the Code changing "storage facilities" to "facilities for the bulk storage of fungible commodities" have greatly restricted that field, making obsolete some of the earlier decisions such as *Catron* and *Central Citrus*. Perhaps the Service feels that this statutory victory makes its concession on the "predominant use" test insignificant. As indicated earlier, it is by no means clear that the 1971 amendments did indeed attempt to constrict and reform the "storage facility" provision; that dispute must, of course, ultimately be resolved by litigation. Regardless of the resolution, it is clear that an analysis of function will remain the keystone of the characterization process for storage facilities: only the breadth of function embraced will be affected. Indeed, the functional analysis flourishes in the area of storage facilities as it does nowhere else in the law of the investment credit.

V. Building and Structural Components

A. Buildings

(1) Legislative History and Regulations

As proposed, section 38 property would have included buildings along with other categories of "other tangible property," thus qualifying for the investment credit if the restrictions on use were complied with.[202] The actual enactment, however, reversed this approach and specifically denied the credit for "buildings" and their "structural components."[203] Perhaps Congress felt that permitting the credit for buildings would prove too inflationary, or would channel capital investment into areas not perceived as requiring the tonic.[204] Whatever the reason, the exclusion has resulted in a monu-

202. Richard, *Is IRS Taking Too Narrow a View on What Qualifies as a "Structure" for Section 38?*, 30 J. Tax. 181 (1969).

203. Int. Rev. Code of 1954, § 48(a)(1)(B).

204. The Committee Reports do not explain. 1962 Report, *supra* note 3, at 415-16.

mental headache for the Service and taxpayers alike, precipitating fierce semantic melees over just what is and what is not a "building" or "structural component" thereof.[205]

The Technical Explanations of the 1962 Revenue Act observe that:

> The term "building" is to be given its commonly accepted meaning, that is, a structure or edifice enclosing a space within its walls, and usually covered by a roof. It is the basic structure of an improvement to land the purpose of which is, for example, to provide shelter or housing or to provide working, office, display, or sales space.[206]

The hope that "building" would be accorded its commonly accepted meaning has proven to be overly optimistic.

In defining building, the regulations basically repeat the language of the Technical Explanations, but rearrange the syntax with the result that two distinct tests for "building" emerge. In stating that "building" "*generally* means any structure or edifice enclosing a space within its walls, and usually covered by a roof"[207] the Service establishes an appearance test that closely approximates what is referred to in the Technical Explanations as the "commonly accepted meaning" of "building." But in the next clause the regulations add a functional test: "the purpose of which is, for example, to provide shelter or housing, or to provide working, office, parking, display or sales space."[208]

The use of "generally" in the clause prescribing the appearance test implies that there will be exceptions to that test; perhaps that language was inserted to provide for such exceptions as "storage" and "research facilities," which obviously look like buildings but nevertheless are permitted to qualify for the credit because of their peculiar function. Under this reading, both the appearance and function tests would have to be met before a structure could be termed a building, thus narrowing the category of buildings. Indeed, this is the sense conveyed by the language of the Technical Explanations, which seem to attribute both the appearance and functional characteristics to the concept of "building."[209] There is another pos-

205. For example, the Rhode Island Investment Credit has chosen not to enter the "what is a building" thicket, providing that property eligible for the credit includes: "tangible personal property and other tangible property, including buildings and structural components of buildings . . . ." R.I. GEN. LAWS ANN. § 44-31-1(a) (Supp. 1974).

206. 1962 TECH. EXPLANATION, *supra* note 10, at 516.

207. Emphasis supplied. The full sentence reads: "The term 'building' generally means 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." Treas. Reg. § 1.48-1(e)(1) (1964).

208. *Id.*

209. *See* note 206 *supra* and accompanying text.

sible reading, however, which broadens "building"—interpreted differently, a structure meeting *either* test constitutes a "building." Thus, under the appearance test, all structures which look like buildings are "buildings" for purposes of section 38; in addition, structures which do not look like buildings, but which nevertheless act like them under the function test, are also "buildings" for which the credit is not available. Because it provides much room for maneuver, this latter reading is preferred by the Service.

The regulations also provide two "special purpose" exceptions to the term "building":

> a structure which is essentially an item of machinery or equipment, [and] a structure which houses property used as an integral part of an activity [which is a qualifying activity for 'other tangible property'] if the use of the structure is so closely related to the use of such property that the structure clearly can be expected to be replaced when the property it initially houses is replaced.[210]

The relationship of these exceptions to the appearance and function tests is not quite clear; for example, is a structure which is essentially an item of machinery or equipment not a "building" even though it provides working space, or would the existence of working space prevent it from qualifying as "essentially an item of machinery"?[211] Equally unclear are the consequences of falling within one of the two exceptions: is a structure that is saved from being a building because essentially an item of machinery or equipment to be considered "tangible personal property,"[212] or "other tangible property" subject to the integral part restriction on use?[213] Further, whatever the answer to that question might be, is the answer the same for an item spared the "building" fate by the other exception, for structures "closely related" to machinery?[214]

(2) The Appearance Test for "Building"

The regulations cite apartment houses, factory and office buildings, warehouses,[215] barns, garages, railway and bus stations, and

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210. Treas. Reg. § 1.48-1(e)(1) (1964).

211. Little clarification was furnished by the legislative history of the 1971 Revenue Act. *See* 1971 REPORT, *supra* note 189, at 29-30.

212. By virtue of the statement in Treas. Reg. § 1.48-1(c) that all items in the nature of machinery are considered tangible personal property.

213. Because an inherently permanent structure. *See* discussion following note 60 *supra*.

214. *See* text accompanying notes 302 et seq. *infra*.

215. "Storage facilities are distinguished from warehouses in that the former are generally structures of any size, shape, or construction designed for bulk storage of fungible commodities (including commodities in liquid or gaseous state). In contrast, warehouses generally are conventional buildings designed for general storage purposes." Rev. Rul. 74-451, 1974 INT. REV. BULL. No. 38, at 7. To say that warehouses are "conventional buildings" comes very close to begging the question.

stores as examples of "buildings,"[216] all of which concededly look like buildings and comport with the common understanding of the term. In an early ruling, the Service applied the appearance test to conclude that a booth for drive-up banking was a "building," observing that the booth enclosed space within its walls and was covered by a roof.[217] On similar reasoning, a "mushroom house" specially designed for and suitable only as a place in which to grow mushrooms was denoted a "building" because of its walls and roof,[218] as were towers housing machinery at a breaker and fine-coal plant,[219] and docking and maintenance facilities at a trucking terminal.[220] An electrical utility's strong "special purpose structure, closely combined with equipment" argument was rejected through application of the appearance test in Revenue Ruling 73-281,[221] denying the credit for enclosures that the taxpayer was required by local zoning ordinances to erect around its transmission substations. Although these enclosures were specially adapted for housing equipment, with reinforced floors and oversize doors for access to the equipment, and though no substantial work activities were carried out therein, the Service's attention was riveted on their exterior resemblance to other, more pedestrian, "buildings" in the area, resulting in disallowance of the credit.

The Service is not above employing something of a "heads-I-win, tails-you-lose" approach in this area, however. Thus, when confronted with structures which apparently do not qualify as buildings under the appearance test, the Service asserts the functional test to support the "building" appellation. Thus, the Service has termed "buildings" a structure supporting an overhead crane[222] and a baseball stadium[223] even though the former had neither floor nor sides, and the latter no roof. In perhaps the most interesting departure from the appearance test, Revenue Ruling 68-530[224] reached the novel conclusion that a "building" could exist, like Jonah, within the belly of another "building": considering "clean rooms" built within a factory for the dust-free testing of electronic equipment,

216. Treas. Reg. § 1.48-1(e)(1) (1964).

217. Rev. Rul. 65-79, 1965-1 CUM. BULL. 26. Note also that the purpose of this booth was to provide working space, a most important indicium of a "building" under the functional analysis. *See* note 246 *infra* and accompanying text.

218. Rev. Rul. 66-156, 1966-1 CUM. BULL. 11.

219. Rev. Rul. 68-50, 1968-1 CUM. BULL. 364.

220. Rev. Rul. 71-203, 1971-1 CUM. BULL. 7.

221. 1973-2 CUM. BULL. 7. This argument was also made without success in the case of a building converted to a cold-storage warehouse through the addition of refrigeration equipment and superheavy insulation. Rev. Rul. 68-405, 1968-2 CUM. BULL. 35.

222. Rev. Rul. 68-209, 1968-1 CUM. BULL. 16.

223. Rev. Rul. 69-170, 1969-1 CUM. BULL. 28.

224. 1968-2 CUM. BULL. 37.

the Service maintained that "[t]he fact that the 'clean rooms' are contained within a larger building and were constructed so as to provide a controlled temperature, humidity, and dust-free environment does not keep them from coming within the definition of the term 'buildings'. . . ."[225]

Early court decisions in the area accorded great weight to the appearance test, although the cases generally dealt with structures which qualified as "buildings" under both the appearance and the function tests. Thus, in *Sunnyside Nurseries, Inc.*[226] and *Arne Thirup*,[227] the Tax Court noted that the taxpayers' greenhouses, in terms of their physical appearance and function, were clearly buildings within the common understanding of that term. Other decisions, however, have de-emphasized the appearance test in situations where that test pointed to "building," but the function test did not. In *Brown-Forman Distillers Corp. v. United States*[228] the Court of Claims allowed the credit for six whiskey maturation facilities because of their special function despite their physical resemblance to "buildings," noting sarcastically that:

> [The Commissioner's position is] premised essentially on what might be called a "look-alike" argument, i.e., since the facilities look like buildings, they must be *ipso facto* buildings as that term is used in section 48(a)(1)(B). Strangely enough, this position is in direct contradiction to a consistent pattern developed by [the Commissioner's] own ruling.[229]

And in *Melvin Satrum*[230] the Tax Court noted that "it is clear that the courts have concluded that certain structures, though outwardly resembling buildings, were not considered so for purposes of section 48(a)(1)(B)."[231] That decision permitted the credit on a functional analysis for an automated poultry raising facility,[232] despite one judge's complaint that his rural heritage had always taught him that a henhouse was "really and truly a 'building'," infected with "the unmistakable look of a building."[233] It is perhaps too early to speculate on the future of the appearance test. If nothing else, it serves as a valuable link between the rarified and often hypertechnical world of tax definitions and the more prosaic world of common sense and common understanding. But *Brown-Forman* and *Satrum* seem to be the beginnings of a trend away from this

225. *Id.* at 38.
226. 59 T.C. 113 (1972).
227. 59 T.C. 122 (1972) (decided the same day as *Sunnyside*).
228. 74-2 U.S. Tax. Cas. ¶ 9592 (Ct. Cl. 1974).
229. *Id.* at 84,911.
230. 62 T.C. 413 (1974).
231. *Id.* at 416.
232. *See* text accompanying notes 257 & 300 *infra*.
233. 62 T.C. at 420 (Dawson, J., dissenting).

emphasis on appearance. The law may be moving toward the point where both the appearance and the function tests must be satisfied before the Commissioner will be permitted to refuse the credit on the ground that a structure under consideration is a "building," or future development may indicate that the appearance test will be totally overshadowed and replaced by the functional test.

(3) The Function Test for "Building"

An inquiry into the function of a structure is quite a realistic approach to its categorization for purposes of the investment credit.[234] Indeed, at times the Service has noted that "the definition of the term building for investment credit purposes is stated in terms of function rather than physical appearance."[235] While this probably overstates the Service's general position,[236] an analysis of function is certainly a major element of the decision whether a structure will be disallowed the credit because it is a building. The regulations observe that structures which provide shelter or housing, or working, office, parking, display, or sales space are performing the archetypal functions of a "building."[237]

The Revenue Rulings have classified numerous structures as buildings because their purpose and function was to provide shelter. An early ruling disallowed the credit for a steel structure providing an automated system for the care, feeding, and raising of hogs through their maturity because it served as a "shelter" for the hogs.[238] Airplane hangars similarly have been denied the credit as buildings by virtue of the parking space and shelter they provide for aircraft and mechanics.[239] A somewhat less convincing ruling disqualified a covered grandstand because it provided shelter for patrons of a racetrack.[240] Although all of the aforementioned examples provided at least some shelter for living creatures, a structure may be disqualified if it provides shelter for machinery alone, even with-

234. Especially in the case of a "storage facility," where an examination of function may be the only means of telling such a facility from a "warehouse." *See* Robert E. Catron, 50 T.C. 306 (1968); Rev. Rul. 74-451, 1974 INT. REV. BULL. No. 38, at 7.

235. Rev. Rul. 68-209, 1968-1 CUM. BULL. 16,17.

236. This ruling dealt with a "storage facility"; the analysis is not necessarily the same for all buildings. See note 234 *supra* and CONCLUSION *infra*.

237. Treas. Reg. § 1.48-1(e)(1) (1964).

238. Rev. Rul. 66-329, 1966-2 CUM. BULL. 16. This ruling was disapproved in the Senate Finance Committee Report on the 1971 Revenue Act. 1971 REPORT, *supra* note 189, at 29-30.

239. Rev. Rul. 66-329, 1969-1 CUM. BULL. 30.

240. Rev. Rul. 69-614, 1969-2 CUM. BULL. 8. The result is probably correct, but the emphasis on providing spectator shelter is unfortunate and possibly misleading. A grandstand of sturdy construction would likely be considered a building with or without a shelter-providing roof. *See* notes 259-60 and accompanying text *infra*.

out space for humans to move around in inside.[241] This does not necessarily mean that any roofed structure is subject to the charge that it does, or could, provide shelter for someone or something, and is, therefore, a "building": Revenue Ruling 68-345[242] stopped short of using this rationale with metal canopies erected over the pump islands of service stations, probably because such canopies are clearly beyond the pale of the "common understanding" of the term "building." Nevertheless, one suspects that the Service would have been tempted to characterize the canopies as buildings had they been employed in an activity which, unlike retail gasoline selling, would have otherwise qualified them for the credit if "other tangible property."[243]

Perhaps the most commonly invoked functional rubric is the characterization of a structure as a "building" because it provides "working space." The existence of working space, apparently without distinguishing between actual work space and space where work merely *could* be conducted,[244] serves, for example, to distinguish between qualifying "storage facilities" and ineligible "warehouses."[245] "Work" generally refers to any sort of human employment or endeavor, although an inquiry into the quantum of the activity conducted is appropriate. A structure whose principal purpose is to provide space for work will not be eligible for the credit; an obvious example is a factory building.[246] A less obvious example is the "clean room," which although it appeared to be a large piece of equipment, was nevertheless disqualified.[247]

Even if the principal purpose of the structure is to provide space for something *other* than human work, the Service will disallow the credit for any areas of the structure where a substantial amount of work is performed that can be conceptually separated from the rest; an example is Revenue Ruling 69-412,[248] in which the Service approved the credit for a structure enclosing an electrical generating station (as closely combined with machinery), but denied it for one

241. Rev. Rul. 72-398, 1972-2 CUM. BULL. 9 (blockhouse for antenna relay and switching equipment, witb bardly room to move around inside, is a "building").

242. 1968-2 CUM. BULL. 30.

243. *Cf.* Rev. Rul. 68-209, 1968-1 CUM. BULL. 16 (craneway is a building, and is ineligible for the credit even though engaged in an otherwise qualifying activity).

244. *Compare* Palmer Olson, 29 CCH Tax Ct. Mem. 1367 (1970) (work *could* be performed within structure, so it is a "building") *with* Rev. Rul. 66-89, 1966-1 CUM. BULL. 7 (work *is* being performed inside structure in question, making it a "building").

245. *See generally* Rev. Rul. 74-451, 1974 INT. REV. BULL. No. 38, at 7.

246. Rev. Rul. 66-299, 1966-2 CUM. BULL. 14. There was, however, a legitimate issue as to whether the factory nevertheless should be credited because "closely combined" with machinery housed therein. *See* text following note 286 *infra*.

247. Rev. Rul. 68-530, 1968-2 CUM. BULL. 37.

248. 1969-2 CUM. BULL. 2.

area devoted to office space.

Sometimes it appears that the Service unduly exaggerates the importance of working space provided by a structure which obviously has some other, more important, function. A striking example is the craneway discussed in Revenue Ruling 68-209.[249] This craneway, providing a track for a movable overhead crane, had a roof and mounted light fixtures, but had no sides and only a dirt floor. The Service nevertheless concluded that the craneway was a "building" because it provided shelter and working space under the roof (which was apparently added chiefly to absorb stress placed on the structure by the cranes) for employees to carry on tasks related to the assembly of the taxpayer's product. Indeed, the Service is more interested in the quantum of work carried on in the structure than in the relation of that work to the principal purpose of the structure. Just as the craneway was labeled a building because the Service felt that a substantial amount of activity, although unrelated to the purpose of the structure, took place therein, a structure housing the generator and propulsion turbines at a hydroelectric site escaped characterization as a "building" despite the fact that maintenance and repair work was intended to be performed inside because that work was found insubstantial, and therefore "incidental."[250] Naturally, a taxpayer is on much safer ground if no work whatever is carried on within the structure.[251]

The courts have largely agreed with the Commissioner's analysis, frequently pointing to the existence or lack of working space as key elements in the decision that a structure is or is not a building. The Tax Court in *Sunnyside Nurseries*[252] and *Arne Thirup*[253] rejected some plausible arguments advanced by the taxpayers for the proposition that their automated greenhouses should be considered items of equipment; the basis for the rejection was the large amount of human activity which took place within the structures. The court noted in *Sunnyside* that "a corps" of the taxpayer's employees, often fifty at a time, carried out all sorts of activities inside the greenhouses, and that this characteristic of "frequent and regular human occupation" (even though "supplemental" to the main purpose of providing a controlled environment) served to defeat the owner's contention that the greenhouses were merely large processing chambers.[254] In *Thirup*, decided on the same day as

249. 1968-1 CUM. BULL. 16.
250. Rev. Rul. 72-223, 1972-1 CUM. BULL. 17.
251. Rev. Rul. 71-104, 1971-1 CUM. BULL. 5.
252. 59 T.C. 113 (1972).
253. 59 T.C. 122 (1972).
254. 59 T.C. 113, 119-20.

Sunnyside, the court conceded that the greenhouses were less substantial and "building-like" than those in its companion case, but concluded nevertheless that they properly were classified as "buildings" because of the substantial number of persons who were occupied therein for no less than five full work days per week.[255] It will also be recalled that in *Catron*[256] the court distinguished the area of the quonset hut which could qualify as a storage facility from the remainder of the structure by the extent of the work done in each part, and permitted a small amount of "incidental" work (the movement of goods to and from storage) to be carried on within the storage area.

To the same effect is the recent decision in *Melvin Satrum*.[257] Satrum's automated poultry facilities contained space between the chicken cages where humans could walk, and various individuals did perform some tasks inside, such as collecting eggs, feeding the birds, and removing droppings; the total time spent was perhaps six man-hours per day. The Tax Court majority adverted to the difficulty of locating the point on the spectrum between providing no working space and providing such a quantum of space for workers that a structure becomes a "building," but concluded that the work done by humans in these henhouses was insufficient to be more than incidental to the main "production work performed therein by the chickens which was, to state it in the vernacular, what the facility was all about."[258]

While providing space for shelter or work is the most frequently encountered use of structures that invokes the "building" classification under the function test, it is certainly not the only one. One of the factors pointed to by the Service in denoting a baseball stadium a "building" was its function of furnishing spectator space.[259] This is a more satisfactory and consistent rationale for the classification of sports facilities, most of which are within the common understanding of "building" anyway, than is an emphasis on affording

255. 59 T.C. 122, 127-28.

256. Robert E. Catron, 50 T.C. 306 (1968), *acquiesced in*, 1972 INT. REV. BULL. No. 44, at 5. *See* text accompanying notes 168-74 *supra*.

257. CCH TAX CT. REP. ¶ 32,665 (1974).

258. *Id.* at 2756. Note that tbe Tax Court considered both the amount of work in absolute terms and its nexus to the main purpose of the facility. See notes 249-50 and accompanying text *supra*. The dissenting judges strenuously objected that the degree of human activity carried on in *Satrum* was indistinguishable from that which had resulted in the classification of the greenhouses in *Sunnyside* and *Thirup* as buildings, emphasizing that the work done in the henhouses was conducted on a daily basis, was indispensible to the operation, and was "substantial." CCH TAX CT. REP. ¶ 32,665 at 2757 (1974) (Dawson, J., joined by Raum & Drennen, JJ., dissenting). In any event, the dissent asserted that there was at least as much work done in *Satrum's* poultry houses as there was in "any barn, which is plainly a building within the meaning of the statute."

259. Rev. Rul. 69-170, 1969-1 CUM. BULL. 28.

shelter for spectators.[260]

A creative argument sometimes advanced by the Service in an attempt to expand the function analysis is to maintain that a structure is a building because it "provides space for the ordinary functions of buildings." The Service originally may have intended this formulation as a short-hand expression for some of the other, already detailed, functions, but it is an unfortunate phrasing: it is vague; it is circular in the implied conclusion that a building is a building because it is a building; and it may serve as a smokescreen concealing either a lack of analysis, an expansion of the "building" concept, or both. This formulation was harmlessly employed in Revenue Ruling 73-281,[261] dealing with enclosures built by an electric utility under local zoning ordinances to camouflage its transformers and relay substations by making them resemble other buildings in the neighborhood. The structures looked like buildings, but the Service was not content to rest its decision that they *were* "buildings" on the appearance test; although it could point to no human activity inside, the Service bravely concluded that "the enclosures are structures, enclosing space within their walls, that provide the ordinary functions of a building."[262] The reasoning is insubstantial, and the ruling illustrates the virtues of leaving well enough alone.

Probably the most objectionable applications of the function test by the Service have come in cases involving mobile homes and other trailers. Revenue Ruling 67-156[263] concluded that a motor vehicle trailer used as a laundrette at a mobile home park was a "building" by employing the same sort of reasoning that failed the Commissioner concerning the floating docks in *Morgan*:[264] if an impermanent asset is employed in the same manner as another more permanent one, then the classification applied to the more permanent asset for investment credit purposes should be applied by analogy to the less permanent one. Here, the Service concluded that since most laundrettes were contained in "building," trailers used as laundrettes should be considered "buildings," too, despite the unbuilding-like characteristic of mobility.[265] After this Nijinskian

260. This seems a more satisfactory rationale than that employed in Rev. Rul. 69-614, *supra* note 240. The discussion is important only as a matter of logical consistency, however, since these facilities would not likely qualify for the credit even if they escaped the "building" characterization, because the presentation of sporting events is not a qualifying activity for "other tangible property," and only a strained construction of "tangible personal property" could embrace these structures.

261. 1973-2 CUM. BULL. 8.

262. *Id.* For a fuller statement of the facts of this ruling, see text following note 221 *supra*.

263. 1967-1 CUM. BULL. 7.

264. *See* text following note 114 *supra*.

265. The Service lamely attempted to explain away the problem of mobility by stating

leap, it would be but a short step to conclude that a circus tent is also a "building."

The Commissioner employed the analogy of function rationale to assert before an unimpressed Tax Court that a house trailer was a building in *Joseph H. Moore*.[266] The Tax Court observed:

> The regulations cite "buildings or *other* inherently permanent structures" as examples of improvements to land, indicating that in order to fit the definition of a building, an item of property must be an inherently permanent structure on the land. [citation omitted]. It is apparent that the trailers in the instant case do not fit this description.[267]

The court required that "before the 'functional use' test can properly be applied . . . it must first be shown that the trailers were permanent improvements to land,"[268] and the court concluded they were not.[269] This holding that simply to perform the function of a more permanent building does not a building make is a most reasonable rejection of a hypertechnical and fictional approach to an area already exhibiting a marked divergence from real-world considerations.

Indeed, the most serious difficulty with the functional analysis is that the test, which began as an attempt to inject a realistic consideration into the characterization process, shows signs of ultimately developing into the vehicle which will eliminate reality as an element of the decision. To the extent that analysis of and analogies concerning a structure's use come to overshadow and replace examination of its appearance, there is a danger of excessive resort to fictions through the conversion of ordinary words into legal cant. A building in law may come to bear less and less resemblance to its counterpart in fact. There are already ample indications of such a drift. One example is the strained analogy employed in the attempt to characterize trailers as "buildings," which glosses over the problem that the trailer's mobility is totally inconsistent with the common understanding of a building. Another difficulty becomes appar-

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that: "[a]n asset which has mobility characteristics is not automatically excluded from the category of buildings. . . . Its *actual* functional use rather than its possible use will be controlling." 1967-1 CUM. BULL. 7,8 [emphasis added]. Farmer Olson doubtless would have made good use of this language had he been aware of it (illustrating the folly of pro se tax litigation) in the case of his quonset huts, which were banished from the garden of "storage facilities" not because an objectionable use *was* being made of them, but because it *could* have been. Palmer Olson, 29 CCH Tax Ct. Mem. 1367 (1970).

266. 58 T.C. 1045 (1972), *aff'd*, 74-1 U.S. Tax Cas. ¶ 9146 (5th Cir. 1973) (per curiam).

267. 58 T.C. 1045, 1051-52 (the emphasis is the court's).

268. *Id.* at 1053.

269. By having the trailers classified as tangible personal property, the taxpayer won the battle. The Service won the war, however: it was determined that the trailers were ineligible for the credit because within § 48(a)(3)'s exclusion of property used predominantly for furnishing lodging. *Id.*

ent by juxtaposing Revenue Ruling 68-209[270] and *Satrum*[271]: a layman would surely marvel at the sophisticated legal metaphysics producing the conundrum that a craneway lacking floor or sides is a "building," whereas a henhouse possessing both is not.

Symptomatic of the attitude underlying this overzealous application of a functional analysis is the curt rejection in *Brown-Forman* of the Commissioner's attempt to interest the Court of Claims in the dictionary definition of "building." Reciting Judge Learned Hand's familiar admonition about fortresses and dictionaries, the court observed that:

> those definitions are of little help in the task of construing the statutory word . . . . The architect tends to define "building" in terms of a common-features rationale rather than on a consideration of the structure's function or use . . . [which] is the more important criterion.[272]

To first analyze function rather than physical features, as the court says, may be the desirable methodology; but to reject all consideration of physical features or common understanding, as the court does, is shortsighted oversimplification. The Technical Explanations to the 1962 Revenue Act established the "common understanding" of the term "building" as the guideline for the resolution of difficult issues; one wonders what quicker way exists to discover the common understanding of a term than to consult the dictionary. One is led inescapably to the conclusion that in *Brown-Forman* the Commissioner was right, and the court wrong, on the issue of the relevance of the dictionary.

(4) The "Special Purpose" Exceptions

In addition to the appearance and function tests for the isolation and identification of characteristics indicating that a structure is a building, the regulations also provide some special categories of structures that will not be considered buildings for investment credit purposes. Besides storage and research facilities, the regulations state that the term "building" does not include a structure which is essentially an item of machinery or equipment, nor does it include a structure housing property used as an integral part of manufacturing, production, extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services *if* the use of the structure is so closely related to the use of the property contained therein that the structure "clearly can

270. 1968-1 CUM. BULL. 16 (the craneway). *See* text accompanying notes 222 & 249 *supra*.

271. *See* notes 257-58 *supra* and accompanying text.

272. 74-2 U.S. Tax Cas. ¶ 9592 at 84,913.

be expected to be replaced" when the property it initially houses is replaced.[273]

It was not at all clear in the beginning precisely what sort of machinery the Service had in mind in conceiving this exception for equipment which was essentially an item of machinery or equipment and which might be mistaken for a building. Presumably, the structures spoken of should share certain characteristics of other buildings, such as enclosing some sort of space. The "clean rooms" of Revenue Ruling 68-530[274] might have seemed likely candidates for this exception, since they combined qualities smacking of a building (walls, floors, and ceilings) with others consistent with the notion of specialized "equipment" (special construction thoughout and a separate atmospheric control system to ensure a dust-free interior environment), if not "machinery." The Service was unimpressed with this contention, however, and did not even discuss the "machinery or equipment" exception, concluding that the existence of working space within made the clean rooms little "buildings." Nor was the "equipment" issue discussed in Revenue Ruling 68-405,[275] which held that a building converted into a cold storage warehouse by a meat processor who installed refrigeration equipment and heavy insulation, sealing all the doors and windows, nevertheless remained a "building." The taxpayer might have argued that the building was a giant refrigerator, and hence an item of "equipment": if the argument was made, the Service did not dignify it with a reply in the published ruling.

After this inauspicious beginning, however, the Service began to put flesh on the bones of the "machinery or equipment" exception. In Revenue Ruling 69-557[276] a dry kiln structure used by a wooden door and column manufacturer became the first piece of property officially to qualify for the exception. Although the sides, floors, and roofs certainly made the kilns look like buildings, the Service observed that they could provide neither shelter nor working space because of the high temperatures inside; rather, they were

273. Treas. Reg. § 1.48-1(e)(1) (1975). This language is taken from the Senate Finance Committee Report on the 1971 Revenue Act. 1971 REPORT, *supra* note 189, at 29-30. Before 1972, this latter exception read "*must* be replaced." The regulation cites oil and gas storage tanks, grain storage bins, silos (which in any event qualify as facilities for the bulk storage of fungible commodities), fractionating towers, blast furnaces, basic oxygen furnaces, coke ovens, brick kilns, and coal tipples as examples of structures which thus escape from the building rubric, but do not clearly indicate whether each particular example is exempted because "essentially an item of machinery or equipment," or "so closely related" to property used as an integral part of one of the aforementioned activities.

274. 1968-2 CUM. BULL. 37. *See also* text accompanying note 247 *supra*.

275. 1968-2 CUM. BULL. 35.

276. 1969-2 CUM. BULL. 3.

chambers for automatic processing of a product. Concluding that the kilns were essentially indistinguishable except for size from the shells or chambers of ovens, the Service ruled that they were not "buildings" because they were esentially items of machinery or equipment. Somewhat later the Service employed similar reasoning to hold in Revenue Ruling 71-489[277] that refrigerator and freezer structures used in the final processing of dairy products were also essentially items of machinery or equipment rather than "buildings."[278]

Reading these rulings together, one concludes that the "item of machinery or equipment" exception seems to be reserved by the Service for specially constructed processing chambers, although these chambers will qualify for the exception only if the processing is essentially automatic. Any substantial amount of human activity conducted within the chamber will result in its exclusion from the exception and classification as a "building."

Little judicial activity has taken place in the area, although the Court of Claims reached a decision along the above lines in *Brown-Forman Distillers*,[279] holding that the whiskey maturation sheds were essentially items of equipment. The court refused to call them "buildings" because of their functions as mild ovens, cycling the temperature and humidity to control the aging of whiskey in wooden barrels. Significantly, no human work went on inside. Although these maturation sheds do not seem as "mechanical" or machine-like as the dry kilns or freezers, the analogy to those latter items drawn by the court is not unpersuasive.[280]

The second special purpose category of structures which will not be considered buildings is structures so closely related to the use of the property housed inside certain property[281] that they "clearly can be expected" to be replaced contemporaneously with that property.[282] The regulations note that factors indicating that a structure

277. 1971-2 CUM. BULL. 64.

278. Because of the low temperatures inside these structures, the only work carried out within them was the stacking or removal of the commodities brought there to be chilled or frozen.

279. *See* note 238 *supra*.

280. The unpersuasive part of the opinion is the short shrift the court accords appearances. *See* text accompanying note 272 *supra*.

281. The property must be used as an integral part of manufacturing, production, or extraction, or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services. It is not clear in the regulations whether the property itself must be machinery or even "tangible personal property." Treas. Reg. §1.48-1(e)(1) (1975).

282. The regulation reads: "[A] structure which houses property used as an integral part of an activity specified in section 48(a)(1)(B)(i) if the use of the structure is so closely related to the use of such property that the structure clearly can be expected to be replaced when the property it houses eventually is replaced." Treas. Reg. § 1.48-1(e)(1) (1975).

is "closely related to the property it houses" include the fact that the structure is specially designed to provide for the stress or other demands of that property, as well as the fact that the structure could not be used economically for other purposes. The present regulations, amended in 1972,[283] relax the stand taken in the original regulation, which had required that the structure contain "machinery or equipment" (now the term used is the broader "property"), had specified that the structure "must be replaced" (rather than "can be expected to be replaced"), and had required further that the structure be depreciated over the life of the machinery contained therein.[284]

The Service has never generously applied this exception to structures. For example, an attempt to qualify under it was rejected in Revenue Ruling 66-156,[285] involving the "mushroom house." Although the structure would have been quite unsuitable without substantial reconstruction for any purpose other than to provide that dark, dank atmosphere so favored by adolescent mushrooms, the Service read quite literally the requirement then in effect that the structure be closely combined with "machinery" and the result was the conclusion that the house was a "building."[286] Similarly, a factory building carefully constructed around the manufacturing process it housed, with specially designed and placed walls and ceilings, was nevertheless held outside the "closely combined with the machinery" exception. Conceding that the factory had been specially designed to provide for the stress demands of the machinery and equipment installed therein, the Service emphasized that the machinery could be removed and replaced without requiring the total demolition of the building—although an exterior wall or two might need to be torn down to get the machinery out.[287] The Service probably believed that to allow the credit for factory buildings would have created too large a loophole in the general prohibition against allowing the credit for "buildings."

The exception was construed just as narrowly in Revenue Rul-

283. The amendment was announced in T.D. 7203, 1972-1 CUM. BULL. 5.

284. Treas. Reg. § 1.48-1(e)(1) (1975), *promulgated by* T.D. 6731, 1964-1 (part 1) CUM. BULL. 11, 37, *as amended*, T.D. 7203, 1972-1 CUM. BULL. 5.

285. 1966-1 CUM. BULL. 11. *See* text accompanying note 218 *supra*.

286. Perhaps there would be a different result if the ruling were requested today, since the reference in the regulations to "machinery" has been changed to "property used as an integral part of an activity specified in section 48(a)(1)(B)(i)," which the mushroom beds plainly seem to be. *See* Treas. Reg. § 1.48-1(d)(4) (1975).

287. Rev. Rul. 66-299, 1966-2 CUM. BULL. 14. This ruling has been criticized by the most prolific commentator in the section 38 property field. Kraus, *Problems in Identifying Section 38 Property*, 127 J. OF ACCOUNTANCY 51, 53 (1969).

ings 68-50[288] and 68-209[289] involving breaker equipment towers at a fine-coal plant and the infamous overhead craneway, respectively. Although the structures in both instances had been specially designed and constructed to support and absorb the stress of the machinery in question, the Service disallowed the credit because the equipment could be replaced without destroying the structures; thus, went the reasoning, they must be "buildings."[290]

By contrast, the Commissioner did approve the credit in Revenue Ruling 66-125[291] for the enclosures built around compressors at a natural gas installation. Replacement of the compressors would have required removal of the enclosure. Since the "total dismantling" test, as it might be termed, was satisfied, the enclosures were not deemed "buildings."[292] A more recent ruling[293] shows that considerations other than the extent of dismantling required are also relevant. The structure there in question housed the generator and propulsion turbine of a hydroelectric facility. In approving the credit the Service cited the difficulty of removal of the generator and turbines, but also remarked on the functional integration between the structure, turbines, and generator, as well as their interrelationship in terms of useful life, structure, and design. This shift in emphasis to an appreciation of the continuing utility (or futility) of the structure if separated from its equipment is an advance from the "total destruction" test.[294]

Taxpayers complaining that the Commissioner is being too tight-fisted with this exception have received mixed reactions in the

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288. 1968-1 CUM. BULL. 364.

289. 1968-1 CUM. BULL. 16.

290. Similar reasoning was employed in Rev. Rul. 72-398, 1972-2 CUM. BULL. 9, to deny the credit for blockhouses enclosing antenna relay equipment.

291. 1966-2 CUM. BULL. 17.

292. The credit was also allowed for the metallic skin covering constructed around a massive assembly at an electrical power plant in Revenue Ruling 69-412, 1969-2 CUM. BULL. 2. The skin and the structural elements supporting it were considered an integral part of the boiler assembly on much the same reasoning as in the case of the enclosures around the compressors at the natural gas plant: complete dismantling of the coverings would have been required for replacement of the sheltered machinery.

293. Rev. Rul. 72-223, 1972-1 CUM. BULL. 17.

294. Although the Service revised the wording of the regulations dealing with the "closely related" exception to "buildings" in 1972, it does not seem to have revised its thinking on the matter to any great degree. For example, in a ruling issued after the change in the regulations, Rev. Rul. 73-281, 1973-2 CUM. BULL. 8, the Service placed the "building" label on enclosures for electrical transmission substations. For a fuller explication of the facts, see the text accompanying note 221 *supra*. In so doing it relied on another ruling issued *before* the change, Rev. Rul. 72-398, 1972-2 CUM. BULL. 9, which had grounded *its* decision on the failure of the taxpayer to convince the Service that the structure "must" be replaced (in the words of the old regulation) concurrently with the machinery housed therein. The Service apparently sees little difference between "must be replaced" and "clearly can be expected to be replaced."

courts. In *Walton Mill, Inc.*[295] the Tax Court rebuffed the taxpayer's attempt to characterize a structure housing special air conditioning equipment as "an enclosure closely combined with machinery," emphasizing the taxpayer's failure to show either that the structure could serve no other purpose or that it would have to be retired contemporaneously with the equipment contained within.[296] Other decisions have been more sympathetic to the taxpayer. In *Adolph Coors Co.*[297] the credit was permitted for two heavily insulated beer cellars containing "a honeycomb" of fermentation and storage tanks. It appears, though there was very little discussion of the issue, that the most important factors influencing the decision to include the cellars within the exception were the sheer mass of the equipment located within the cellar, and the importance of the insulation in the walls to the maintenance of the temperature required for proper brewing.

In a more recent decision favorable to the taxpayer, the Court of Claims in *Brown-Forman* concluded (among other things)[298] that the whiskey maturation facility in question met the "closely combined with" exception because the sheds would need to be retired contemporaneously with the maze of whiskey barrel ricks they contained. This is much more liberal than the Commissioner's interpretation of the exception, since the ricks probably could have been removed with no more difficulty than would have attended the removal of the growing beds from the mushroom house; in addition, there was certainly not the same degree of interrelationship of function and interdependence of design between the maturation sheds and whiskey ricks as there was between the metal-concrete enclosures and the generators and turbines at the hydroelectric facility.

The Commissioner received an equally unpleasant jolt from the judicial resolution of the status of *Melvin Satrum's*[299] automated henhouses. After concluding that there was no disqualifying human working space in these facilities (because, to mix a metaphor, the lion's share of the work was being done by chickens), the Tax Court noted that the Senate Finance Committee Report on the 1971 Revenue Act[300] stated that specific design of a structure to provide for the demands of equipment which it houses and lack of any other practi-

295. 31 CCH Tax Ct. Mem. 75 (1972).

296. *See also* William K. Coors, 60 T.C. 368 (1973) (a "saw room" containing the machinery to remove the tops of wooden cartons used by a brewery does not come within the exception because its useful life does not mirror the useful life of the sawing equipment).

297. 27 CCH Tax Ct. Mem. 1351 (1968).

298. The court also held that the sheds were qualifying storage facilities, and were in addition "essentially items of equipment." *See* note 238 *supra* and accompanying text.

299. *See* notes 240-43 *supra* and accompanying text.

300. 1971 REPORT, *supra* note 189, at 29-30.

cal use are important factors in determining that a structure is not a "building." The Tax Court found that the presence of these factors made the henhouse an integral part of the producing process and thus concluded it was not a building. This is a very significant loosening of the "closely related exception," expanding it from a structure built so closely around machinery that it must be torn down to get that machinery out (the Service's view) to encompass virtually any structure specially designed to serve as an integral part of some manufacturing, production, or extraction process. If *Satrum* marks the beginning of a judicial trend, the emphasis in the future will rest much more heavily on the positive elements of uniqueness of design and features than on such negative aspects as unsuitability for other uses and impossibility of removal of property contained inside.[301]

These problems with the breadth of the two special purpose exceptions are most perplexing. Unfortunately, they are not the only problems with the exceptions. Assume, for example, that a structure is found not to be a building because it falls within the first special purpose exception in the regulations as "essentially an item of machinery or equipment." Is the structure to be classed as "tangible personal property?" The regulations state that "all property which is in the nature of machinery" is tangible personal property;[302] but the regulations *also* provide that " 'tangible personal property' means any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures."[303] Although the hypothesized structure is not a technical "building" it probably does have the earmarks of inherent permanence. This presents an annoying riddle: the structure must be tangible personal property, but it cannot be. The Service has not handed down a ruling dealing with the problem, since the structures allowed the credit by the rulings as "essentially items of machinery or equipment" were all employed in activities which would have qualified them for the credit even if they had been "other tangible prop-

301. A dissenting judge, adopting the Service's position in the mushroom house and factory ruling, complained that this approach placed undue emphasis on special design: "In any modern commercial operation, whether it be producing eggs, cows' milk, or manufacturing television sets, the building which houses the operation may be specially designed for that purpose. Its utility for any other purpose will be limited. The equipment in question will be attached to the building. None of these considerations make the structure any less a building as the term is commonly understood." CCH TAX CT. REP. ¶ 32,665 at 2757 (1974) (Quealy, J., dissenting). And if there were any doubt of the matter after the amendment of the regulations, *Satrum* makes clear that the structure need not house *machinery* to come within the "closely related" exception: by no feat of semantics can double-decker coops for 20,000 chickens, or the chickens themselves be classified as "machinery."

302. Treas. Reg. § 1.48-1(c) (1975).

303. *Id.*

erty,"[304] and this mooted the issue of personal property vel non. Suppose, however, that the taxpayer's activity was not a qualifying one. What if a structure is not a technical "building" because essentially an item of machinery, but the taxpayer's business is the furnishing of recreation? In such a situation everything would depend on whether the structure was tangible personal property or not, because tangible personal property qualifies for the credit regardless of the nature of the taxpayer's business activities. The regulations are ambiguous and contradictory.[305]

A similar problem arises in the case of a structure which falls into the second special purpose building exception, for structures "closely related" to the property contained therein, although the resolution is simpler since the 1972 amendments to the regulations. Before the amendments, the regulation spoke of an enclosure "so closely combined with . . . machinery or equipment,"[306] raising the same problem as that presented by the first exception. The present regulations, however, speak of "a structure which houses property used as an integral part of an activity specified in section 48(a)(1)(B)(i)"; since section 48(a)(1)(B)(i) is the section setting forth the activities which qualify other tangible property used as an integral part thereof for the credit, the issue is mooted. The structure will by definition qualify for the credit by virtue of the activity.

While a proposition that both special purpose exceptions should be considered "other tangible property" as a matter of consistency is reasonable and resolves the ambiguity in the regulations, it is certainly not the only permissible resolution, and would likely be vigorously opposed by a taxpayer claiming the credit for a structure "essentially an item of machinery" not engaged in one of the activities set forth in section 48(a)(1)(B)(i).

B. Structural Components

(1) Legislative History and Regulations

All items within or attached to a building except for "structural components" are considered tangible personal property and qualify for the credit regardless of the nature of the taxpayer's business;[307] structural components, like "buildings," never qualify. The Techni-

304. All of these items were involved in "manufacturing, production, or extraction." *See* text following note 276 *supra*.

305. Perhaps the best resolution would be to import the rationale employed in *Weirick* into this area from the realm of the "inherently permanent structure." *See* discussion following note 65 *supra*.

306. Treas. Reg. § 1.48-1(e)(1) (1975), *supra* note 284.

307. Treas. Reg. § 1.48-1(c) (1975).

cal Explanations did not define the term "structural components," but listed "central air-conditioning and heating systems, plumbing, and electric wiring and lighting fixtures, relating to the operation and maintenance of the building"[308] as examples of items comprehended by the term. The original regulations similarly avoided any attempt to define "structural components," but did repeat the characterization "components relating to the operation or maintenance of a building," and provided a comprehensive list of examples.[309] The Revenue Act of 1964[310] overruled the Commissioner's stance on the matter of elevators and escalators, specifically qualifying them for the credit.[311]

(2) Classification of "Structural Components"

The largest category of "structural components," and the characterization most often asserted by the Service, is composed of those items necessary for the "ordinary functions" of a building, an amplification of the phrasing "relating to the operation or maintenance of a building" that appears in the Technical Explanations and regulations. One of the earliest examples of this characterization came in the "mushroom house" ruling.[312] The mushrooms were grown in massive "beds," supported by closely-spaced studs that also supported a false ceiling containing ventilating equipment. The tax-

308. 1962 TECH. EXPLANATION, *supra* note 10, at 503, 516.

309. The list includes:

> walls, partitions, floors, and ceilings, as well as any permanent coverings therefor such as paneling or tiling; windows and doors; all components (whether in, on, or adjacent to the building) of a central air-conditioning or heating system, including motors, compressors, pipes, and ducts; plumbing and plumbing fixtures such as sinks and bathtubs; electric wiring and lighting fixtures; chimneys; stairs, escalators, and elevators, including all components thereof; sprinkler systems; [and] fire escapes . . . .

Treas. Reg. § 1.48-1(e)(2) (1975), *supra* note 284.

310. Act of Feb. 26, 1964, Pub. L. No. 88-272, 78 Stat. 19.

311. The House Ways and Means Committee Report explained: "While these regulations are an accurate interpretation of the intention of Congress last year in this respect, nevertheless your committee believes that it is appropriate to reconsider the treatment of elevators and escalators for purposes of the investment credit." H.R. REP. No. 749, 88th Cong., 1st Sess., 1964-1 (part 2) CUM. BULL. 125, 159. The regulations subsequently were amended to reflect this change in the status of elevators and escalators, T.D. 6838, 1965-2 CUM. BULL. 9, but otherwise were unchanged from those originally adopted on the matter of structural components. Predictably, the Service has made much of the Committee's flattering remark about the accuracy of the regulations' interpretation, often taking the position that this nod of legislative favor has given its interpretation of "structural components" a status as elevated as that of Holy Writ.

See, for example, the Service's arguments in King Radio Corp. v. United States, 73-2 U.S. Tax Cas. ¶ 9766 (10th Cir. 1973); Minot Fed. Sav. & Loan Ass'n v. United States, 435 F.2d 1368 (8th Cir. 1970); Fort Walton Square, Inc., 54 T.C. 653 (1970); and Ponderosa Mouldings, Inc., 53 T.C. 92 (1969).

312. Rev. Rul. 66-156, 1966-1 CUM. BULL. 11.

payer apparently urged that supporting mushroom beds was quite unrelated to the ordinary functions of buildings, and that the studding therefore should not be classified as a structural component. The Service, however, disallowed the credit for the studs because the studding also supported a ceiling (albeit false) generally considered necessary for the ordinary operation of a building. Thus, even if an item serves more than one purpose, the Service will disallow the credit if one of those purposes is consistent with the notion of "structural component."[313]

The Service employed a similar approach in classifying the electrical, plumbing, and sprinkler systems at a factory as structural components, "since they relate generally to the operation of the building as an overall processing operation system."[314] Similarly, even extra-heavy insulation installed to convert a building into a cold-storage warehouse was a structural component in the Service's eyes, because "insulation is a common component of most buildings."[315]

Equally related in the Service's opinion to the ordinary functions, operation, and maintenance of buildings were the custom-designed glass windows at a racetrack grandstand, together with the machinery for raising and lowering them, but *not* the machinery for washing them.[316] Another way to verbalize all this is to identify as structural components all those items "servicing the overall . . . needs of the building system, . . . relating generally to the overall operation of the building,"[317] determined by reference to the platonic archetype of "buildingness" abstracted from the common characteristics of all buildings.[318]

313. This ruling is criticized as overly strict in Kraus, *supra* note 287, at 53.

314. Rev. Rul. 66-299, 1966-2 CUM. BULL. 14, 16.

315. Rev. Rul. 68-405, 1968-2 CUM. BULL. 35, 36. Another taxpayer modernized his factory by adding heavier insulation to the roof and walls and replacing the floors to accommodate newer and heavier machinery, and then cleverly attempted to claim the credit for only the insulation and reinforcing which he considered to be in excess of the requirements of a "normal" factory building. The Service would have none of this, concluding that no allocation was possible in disallowing the credit. Rev. Rul. 69-558, 1969-2 CUM. BULL. 5, 6. This ruling is inconsistent with the decision in *Catron* and, in light of the published acquiesence in that latter case, is possibly no longer reflective of the Service's position. *See* note 319 *infra* and accompanying text.

316. Rev. Rul. 69-614, 1969-2 CUM. BULL. 8. The Service probably based its decision on the observation that almost all buildings have windows and equipment for raising and lowering them, but few buildings have integrated equipment for washing their windows. On the other hand, it could be argued with equal plausibility that very few grandstands have windows, and that very few buildings employ machinery to raise and lower their windows.

317. Rev. Rul. 70-160, 1970-1 CUM. BULL. 7, 8 (describing the electrical system of a building).

318. Or at least all domestic buildings, more precisely (it is doubtful, for example, that flush toilet facilities would be considered common characteristics of all buildings in certain developing countries).

The courts generally have accepted the "relates to the ordinary functions of buildings" phrasing as a reasonable test for structural components. In *Catron* the court disallowed the credit for the "normal" insulation of a building, although it disagreed with the Commissioner's position that the extra insulation installed in the part of the building employed as a cold storage area was similarly a structural component.[319] The court distinguished between nonqualifying items relating to the ordinary operation of most buildings, and qualifying items relating to the particular function of a particular building; the latter category of items are not considered structural components.

The *Central Citrus* court also recognized that distinction in allowing the credit for certain machinery but disallowing it for the electrical equipment used in the general operation of a fruit processing plant, observing that there was

> a clear distinction between property used in the general overall operation of a building, wherein the credit is disallowed . . . and that property which is utilized to aid in the employment of a particular function or particular piece of property.[320]

Naturally, this line is sometimes difficult to draw. In *Ponderosa Mouldings, Inc.*[321] a taxpayer owning a woodworking factory emphasized the great risk of fire peculiar to his business to support an argument that a sprinkler system installed in his factory was too closely related to the manufacturing process to be considered a structural component. The Tax Court saw some merit in the contention, but was persuaded by the Commissioner that, despite the taxpayer's peculiar need for sprinklers, such systems are common enough to be considered structural components related to the ordinary functions of commercial buildings.[322]

A special and prolific subclass of components relating to the ordinary functions of buildings is heating and air conditioning equipment, considered to be structural components in all but the most extraordinary circumstances.[323] The regnlations class only

319. 50 T.C. 306, 316 (1968).

320. 58 T.C. 365, 374 (1972).

321. 53 T.C. 92 (1969).

322. *But cf.* Rev. Rul. 67-417, 1967-2 CUM. BULL. 49, 51 (credit allowed for special fire extinguisher installed near exhaust hood in kitchen of lunch counter because designed for "particular hazard"). Occasionally the judiciary has seemed somewhat overenthusiastic in its application of the "ordinary function—operation and maintenance" test; for example, C.C. Everhart, CCH TAX CT. REP. ¶ 32,241 (1973), concluded that a cesspool located behind a shopping center was a structural component thereof. This was an alternative holding, the other being that the cesspool was "other tangible property" not used within a qualifying activity. Perhaps the court should have confined itself to that latter alternative holding.

323. The original Ways and Means Committee Report spoke of an individual air conditioning unit as tangible personal property (and therefore not a structural component) in

central air conditioning or heating systems as structural components, but a host of rulings have made it plain that the Service's view of "central" is most expansive; indeed, the taxpayer whose air conditioning unit strays ever so slightly from the Commissioner's conception of "individual" will find that the Service is most unsympathetic. The mere fact that an air conditioner is removable without material damage to either the unit or the building does not preclude its disqualification as a structural component,[324] nor is the Service's conception of "central" restricted to a system which controls a building's climate from a single unit located in a single place. The Service maintains that a "central" system may be comprised of a larger number of units, however attached,[325] and that the various components of the system may be dispersed throughout the building without removing it from the category of "central."[326] Perhaps the most extreme example to date is the system classified as "central" in *Fort Walton Square, Inc.*[327] The taxpayer there had installed some thirty air conditioners, each with its own heating and cooling unit, on the roof of his shopping center, with canvas flashing and ducts connecting the units to the areas to be served. The Tax Court concluded that these units together constituted a central system, not individual units, and denied the credit.[328] It seems that a central air conditioning and heating system is defined in negative terms: anything which is not a single window unit is a component of a central system.

The regulations do provide an escape clause for certain heating and air conditioning equipment, however:

> [T]he term 'structural components' does not include machinery the sole justification for the installation of which is the fact that such machinery is required to meet temperature or humidity requirements which are essential for the operation of other machinery or the processing of materials or foodstuffs.[329]

Equipment may qualify under this "sole justification" test even if it incidentally provides for employee comfort, or serves to no more than an insubstantial degree areas where the temperature and humidity requirements are not critical for processing.[330] Machinery thus exempted from the class of structural components by this test

expressing the desire that section 38 property be liberated from the local law of fixtures. 1962 REPORT, 1962-3 CUM. BULL. 405, 415-16.

324. Rev. Rul. 67-359, 1967-2 CUM. BULL. 9, 10.
325. Rev. Rul. 67-417, 1967-2 CUM. BULL. 49, 51.
326. Rev. Rul. 67-433, 1967-2 CUM. BULL. 51-53.
327. 54 T.C. 653 (1970).
328. *Accord*, Kramertown Co., 31 CCH Tax Ct. Mem. 1177 (1972).
329. Treas. Reg. § 1.48-1(e)(2) (1975).
330. *Id.*

is considered tangible personal property.[331] Some examples of property that have been approved for the credit by the Service under the "sole justification" test are: the ceiling mounted refrigeration units, evaporation condensers, compressors, and other cooling equipment installed to convert a building into a cold storage warehouse, together with the specially installed wiring and switches for that machinery;[332] and a boiler and steam plant constructed to raise the humidity within a furniture plant for facilitating the removal of sawdust from the air.[333] The Tax Court employed the "sole justification" test to permit the credit, over the Commissioner's objection, for the extra insulation installed for converting one end of a quonset hut to a cold storage area for apples,[334] and for blowers and coolers installed in "sweet rooms" to control air temperature and humidity, thus retarding the premature ripening of stored fruit.[335]

The "sole justification" test may provide a very narrow bolthole, however: one Tax Court decision limited its application to equipment affecting temperature and humidity, including any other sort of climate control equipment. This case, *William K. Coors*,[336] denied the credit for the duct work of a system installed to remove foreign particles from air before its release into a beer bottling plant, on the grounds that because this system was used neither to heat nor cool the building it perforce fell outside the "sole justification" test. This decision seems clearly erroneous in its draconian interpretation of the exception, and inconsistent with Revenue Ruling 68-530,[337] wherein the Service allowed the credit for climate control machinery which eliminated dust from the air introduced into "clean rooms" for the testing of sensitive electronic devices.[338] Nevertheless, the *Coors* decision is symptomatic of the official attitude which may often cast the taxpayer in the role of the fabled camel forced to traverse a needle's eye in his path to the investment credit.

In addition to the "ordinary function—operation and maintenance" test already discussed, the Service occasionally attempts to characterize components integrated into, but used for the peculiar designed purpose of, a building as "structural components." This is

331. Rev. Rul. 69-558, 1969-2 CUM. BULL. 5, 6.

332. Rev. Rul. 68-405, 1968-2 CUM. BULL. 35-37.

333. Rev. Rul. 70-160, 1970-1 CUM. BULL. 7, 8. Compare this result with William K. Coors, 60 T.C. 368 (1973) and text accompanying note 336 *infra*.

334. Rehert E. Catron, 50 T.C. 306 (1968).

335. Central Citrus Co., 58 T.C. 365, 373-74 (1972).

336. 60 T.C. 368 (1973).

337. 1968-2 CUM. BULL. 37.

338. Concededly the equipment for the "clean rooms" affected temperature as well as particulate content; nevertheless, the latter function was the significant one.

in spite of the early ruling which considered the status of certain property at a bank and which concluded that items attached to the structure whose removal would affect the operations of the structure only as a *bank* (such as vault doors), not as a *building*, could not be considered "structural components."[339] It was not long before the Service lost sight of this distinction. Revenue Ruling 66-156[340] classified the false ceiling in the mushroom house as a structural component, although its only purpose was to house equipment used to create an atmosphere congenial to mushrooms; it was *not* an ordinary ceiling. Recently, the Service classified as structural components canopies attached to a building and which extended out over loading docks to protect certain inventoried manufacturing parts from the elements because they related to the ordinary function and operation of the building.[341] A skeptic might take issue with the Service's assertion that an ordinary function of a building is to protect items left outside it. An even more questionable ruling reached the conclusion that structures for separating the storage areas assigned to various groups of inventoried parts related to "the ordinary function and operation of a building."[342] Removal of these structures would have affected the building's operation as a warehouse but would not have impeded its operation as a building in the general sense.

Those rulings represent a subsurface shift in basic tests. Realizing this, the Service recently recharacterized the test in Revenue Ruling 74-392,[343] classifying loading docks at a factory as structural components because related "to its operation for its *designed* purpose as a factory building."[344] Although this latter "designed purpose" test has not been litigated, it is totally inconsistent with the original "ordinary function" rationale and the earlier conclusion that vault doors are *not* structural components precisely because they were related to the designed purpose of the building as a bank. Carried to its logical conclusion, this new rationale would seem to require classification of the heavy machinery installed in a factory as structural components, because "essential to its operation for its designed purpose as a factory," a result which is obviously at odds with the purpose of the credit. Probably the Service would not assert such an extreme position; nevertheless its consistency with the

339. Rev. Rul. 65-79, 1965-1 CUM. BULL. 26.
340. 1966-1 CUM. BULL. 11.
341. Rev. Rul. 74-2, 1974 INT. REV. BULL. No. 1, at 10, 11.
342. Rev. Rul. 74-3, 1974 INT. REV. BULL. No. 1, at 11-12.
343. 1974 INT. REV. BULL. No. 33, at 6.
344. *Id.* at 17.

"designed purpose" test serves to illustrate the logical difficulty therewith.

Another argument the Service has used on occasion to broaden the reach of "structural components" involves a variation of the same functional analogy attempted with floating docks and trailers:[345] even if an item is impermanent, it should nevertheless be considered a structural component if it performs the same function as its more permanent analog. The reasoning was employed to deny the credit for an air conditioner in Revenue Ruling 67-359,[346] despite the troublesome fact that the unit could easily be removed. A much more blatant example, however, is found in Revenue Ruling 69-14,[347] in which the Service ruled that movable metal partitions, some floor-to-ceiling and others of "bank" (5½ foot) height, were structural components. The Service reasoned that partitions within a building do not need to be permanently anchored to perform the same function as walls; since the partitions were analogous to walls, the Service proposed to treat them like walls.

In *Minot Federal Savings and Loan Association v. United States*[348] the district court totally rejected the Commissioner's analogy between permanent and impermanent walls, noting that the reference in the regulations to "walls, partitions, floors and ceilings" must have been to permanent parts of buildings. The court reminded the Commissioner of the embarrassing inconsistency of his argument with Revenue Ruling 67-349,[349] when the Service had concluded that carpeting was not a structural component because not permanently attached; if lack of permanence saved the carpeting, it also saved the partitions from the "structural components" fate. The Eighth Circuit affirmed,[350] observing that because the building had been constructed and completed without the movable wall dividers, they were no more structural components than were individual air conditioners.

The Commissioner had no better success with this functional analogy in *King Radio Corp. v. United States*,[351] which allowed the credit for similar movable partitions. Indeed, in the *King Radio* opinion the Tenth Circuit announced a new "permanence" test for structural components:

345. *See* text accompanying notes 114 & 263 *supra*.
346. 1967-2 CUM. BULL. 9.
347. 1969-1 CUM. BULL. 26.
348. 313 F. Supp. 294 (D.N.D.), *aff'd* 435 F.2d 1368 (8th Cir. 1970).
349. 1967-2 CUM. BULL. 48.
350. Minot Fed. Sav. & Loan Ass'n v. United States, 435 F.2d 1368 (8th Cir.), *aff'g* 313 F. Supp. 294 (D.N.D. 1970).
351. 73-2 U.S. Tax Cas. ¶ 9766 (10th Cir. 1973).

> We think it was the intent of Congress . . . to exclude from the benefits of [the investment] credit only those [structural components] of a building which are permanent in the sense that they cannot be removed or relocated without doing at least temporary damage to the structure itself.[352]

The court concluded that "structural components" should be restricted to items incorporated within the structure "during the construction phase." This test would change the result of the more restrictive rulings and decisions on removable items, such as air conditioners heretofore glibly categorized as "central."[353] One difficulty with this new test is the problem of determining the scope of the "construction phase." Nevertheless, the court's approach probably comports more closely with the everyday understanding of "structural components" than does the Commissioner's attempt to ignore lack of permanence.[354]

(3) Some Limited Escape Routes

Even if an item is attached to a building with a certain degree of permanence and at first glance looks suspiciously like a structural component, it may still fall within a qualifying exception. One such escape route is provided for heating and air conditioning equipment meeting the already discussed "sole justification" test.[355] Another escape is gained by characterizing the item in question as essentially an item of machinery, or closely combined therewith; although not mentioned in the regulations, an exception has arisen for such property. Whereas the Service will not permit the credit for the general wiring or plumbing system running through a building, it has stated on numerous occasions that it will allow the credit for special connections running directly to a specific item of machinery, conceding that these connections are properly considered parts of machinery.[356]

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352. *Id.* at 82,485. The court also pointed out numerous flaws in the Commissioner's analogy between walls and these partitions, noting that, unlike walls, these partitions were neither an integral part of the structure nor did they bear any of the structural load. *Id.* at 82,484.

353. Such as Rev. Rul. 67-359, 1967-2 CUM. BULL. 9, or Fort Walton Square, 54 T.C. 653 (1970).

354. Indeed, there are signs that even the Service concedes the wisdom of the court's approach; for example, the Service recently placed heavy emphasis on the permanence of a woodblock flooring laid in a factory in determining that the flooring was a structural component. Rev. Rul. 74-391, 1974 INT. REV. BULL. No. 33, at 6. The Service has not asserted this functional analogy between permanent and impermanent assets since *King Radio*. Indeed, it appears from the charge to the jury reported in Fancy Foods of Virginia, Inc. v. United States, 73-1 U.S. Tax Cas. ¶ 9372 (E.D. Va. 1973), that permanence may now be recognized by the Service as one of the necessary attributes of "structural components."

355. *See* text accompanying notes 329-38 *supra*.

356. Rev. Rul. 70-160, 1970-1 CUM. BULL. 7, 8; Rev. Rul. 69-558, 1969-2 CUM. BULL. 5, 7; Rev. Rul. 66-299, 1966-2 CUM. BULL. 14.

This exception to the "structural component" rubric is not confined to plumbing and wiring, however: the Service recently ruled that the credit would be available for a raised floor built over the existing floor of a factory building to permit the emplacement of wiring, air conditioning ducts, and other paraphernalia required for installation of a computer.[357] The Service concluded that because the raised floor was a necessary part of the installation and operation of the computer, it was "essentially an accessory of such equipment," not a structural component of the factory.[358] This is something of a retreat from the Service's earlier tough lines with regard to the false ceiling containing ventilation equipment in the "mushroom house," or the hermetically sealed walls of the "clean rooms."

A final and peculiar exception to "structural components" has been applied thus far only to items of heating equipment leased to building owners by gas utility taxpayers. Normally, gas storage tanks, water heaters and softeners, and the associated tubes, fittings and the like are classified as structural components when permanently installed for use as part of a heating and plumbing system. The Service recognizes, however, that it would be anomalous to deny the credit for such items to a utility which merely leases this equipment to its customers: it seems unfair to disallow the credit to *A*'s property as a structural component of *B*'s building, and so the Service permits the utility to claim the credit where it retains title to the equipment and it seems reasonably possible that the apparatus could be removed on the expiration of the lease.[359]

C. Conclusion: Building and Structural Components

"Building" and "structural components" have engendered a disproportionate amount of confusion for an eight word parenthetical exception to otherwise qualifying "other tangible property." The stakes involved are high: if "other tangible property" can be characterized as a "building," or if accessories can be classified as "structural components" of a "building," the credit irrevocably is lost, and no further argument about specialized uses or the policy of the credit is of any avail. Most of the problems with the term "building" can be traced to the Service's notion that "appearance" and "function" should be considered two different tests, and that a structure

357. Rev. Rul. 74-391, 1974 INT. REV. BULL. No. 33, at 6.

358. The same ruling went so far as to hold that catwalks designed and constructed to provide access for inspection and repair of certain items of equipment would be allowed the credit as "necessary and identifiable" parts of that equipment.

359. Rev. Rul. 70-236, 1970-1 CUM. BULL. 8; Rev. Rul. 69-602, 1969-2 CUM. BULL. 6.

need only meet one to qualify as a technical "building." On the contrary, a structure should not be classified as a building unless it passes *both* tests.[360]

The confusion is compounded by the attitude evidenced by both the courts and the Service that the function test, emphasizing the presence or absence of space for shelter or working areas and minimizing the importance of a consideration of appearances, is the determinative test. Function is, of course, important—but this is *not* to say that it should be the only relevant consideration; placing undue weight on function and ignoring physical nature leads to hypertechnical results (a greenhouse is a building but a henhouse is not) and to unconvincing distinctions. If *Brown-Forman* and *Weirick* seem excessively solicitous of taxpayers' investments with their constrictions of "building," they are balanced by the Commissioner's intransigence with respect to the "special purpose" structure exceptions for edifices "essentially items of machinery" or "closely related to property used as an integral part of qualifying activities, which clearly can be expected to be replaced concurrently with that property." The Commissioner excludes structures from the first exception if they provide working space, and from the second if removal of the equipment contained therein does not necessitate total dismantling of the surrounding structure. Both positions seem too restrictive.

There is also confusion over the scope of "structural components." The earliest rulings applied this characterization only to those components associated with the ordinary functions of buildings generally, such as floors, roofs, permanent walls, and the like, excluding from this category items related more closely to the particular use the taxpayer made of the building, such as bank vault doors. More recently, the Service has moved away from that distinction, sweeping within "structural components" certain items obviously installed only because of the particular needs of the taxpayer, such as extra-heavy insulation for conversion of a building to a cold storage warehouse, and partitions erected within a warehouse to facilitate the segregation of inventoried parts. This trend has not been challenged in the courts, but one might speculate that this new approach would suffer the same judicial fate as did the stretched functional analogy which attempted to convert portable partitions into "structural components."

Equally at variance with the policy of the credit is the Service's overly expansive interpretation of "central" air conditioning, and

360. To illustrate, an adoption of this view would have precluded the surprising ruling that a craneway was a "building."

the sort of limited reasoning which excludes air cleaning equipment from the "sole justification" test for climate control machinery on the grounds that such cleaning machinery affects neither temperature nor humidity. The area might be less encumbered with technical traps for the unwary if the Service would make wider use of the sort of realistic approach which permitted the credit for raised flooring and catwalks installed to facilitate the operation of a computer. These items related to the taxpayer's particular activities, not to the "ordinary functions" of buildings, and were properly excluded from the category of "structural components."

VI. Conclusion: A Suggested Methodology for Section 38 Problems

The identification of section 38 property is a complicated and often frustrating task. Despite such optimistic pronouncements in the legislative history to the effect that tangible personal property would not be construed narrowly, or that "building" would be accorded its commonly understood meaning, the law has developed otherwise. The Service is most reluctant to classify assets as tangible personal property, it seems, and the term "building" is so encrusted with legal barnacles as to be unrecognizable. Rather than wandering once more through the details of the law underlying (and sometimes overgrowing) the various definitional concepts of section 38 property, it would seem more profitable to concentrate on trends which seem to be, or perhaps should be, developing in some of the more troublesome areas.

A. Consideration of Form, Function, and Permanence

The key to understanding section 38 property is an appreciation of the proper interrelationship between form, function, and permanence. Much of the confusion in the area stems, for example, from the Service's free-wheeling employment of the "inherently permanent structure" characterization. Few would argue that a permanent, nonfloating dock is an inherently permanent structure. Problems are created, however, when there is an attempt to apply the same appellation to a floating dock simply because it performs the same function as a nonfloating one: although the function is the same, the form and degree of permanence differ. The proper resolution, as adopted by the courts, is to apply a different characterization. Similarly, the simple fact that an item is attached to the realty does not compel the conclusion that it is an "inherently permanent structure:" it has the form of one, since it is so attached, but inquiry must still be made into its function and degree of permanence. The

courts have demonstrated an appreciation of this. Finally, even though an item seems to be an improvement to land because permanently annexed to the realty, it still should not necessarily be characterized as "other tangible property": like the chair lift towers in *Weirick*, an inquiry into form and function may indicate that it is nevertheless tangible personal property because it is essentially an item of machinery. It is further suggested that *Weirick*'s resolution of this issue—that an inherently permanent structure which is essentially an item of machinery should be considered tangible personal property—is the correct resolution, and that *Roberts* was erroneously decided.

Nor should this tripartite inquiry into form, function, and permanence be confined to inherently permanent structures. A realization that there was more to the inquiry than simply an examination of function led to the very sensible results in *Minot* and *King Radio* that movable wall partitions are *not* structural components. However, it is submitted that the rationale expressed in *King Radio* to the effect that permanence is the sole relevant consideration commits again the error of tunnel-vision, differing from the Service's discredited position in those cases only by a substitution of the permanence tunnel for the functional one.

B. The Function Fallacy

The confusion over the proper role of function probably stems from the emphasis placed on that factor in decisions and rulings dealing with storage facilities.[361] Most of these devoted virtually their entire attention to an analysis of this one factor. But this does *not* mean that they stand for the proposition that an inquiry into function is the only pat answer to all section 38 property problems. Indeed, a little reflection demonstrates that in the particular area of storage facilities (or facilities for the bulk storage of fungible commodities, as they are now styled) function plays the leading role because it is the only variable in the equation: form and permanence are constants. That is, almost all storage facilities are walled structures with roofs, of sturdy construction. Thus, there is no reason to inquire into form and permanence *with this type of property*, and

361. For example, consider the following language from *Satrum*: "While the legislative history of the investment credit indicates that 'building' is to be given its commonly accepted meaning [citations omitted], it is clear that the courts have long concluded that certain structures, though outwardly resembling buildings were not considered so for purposes of section 48(a)(1)(B). Brown & William Tobacco Corp. v. United States, 369 F. Supp. 1283 (W.D. Ky. 1973) (tobacco sheds), and Robert E. Catron, 50 T.C. 306 (1968) (refrigerated portion of corrugated metal quonset hut)." CCH TAX CT. REP. ¶ 32,665 at 2755 (1974). Note that both cases cited by the court were decisions involving storage facilities.

therefore the attention is quite rightly centered on function. To the extent, however, that form and permanence do begin to vary as the consideration moves on to other types of assets, then these elements must also be examined.

So it is with buildings which are not storage facilities. Here, permanence is assumed. Form and function vary greatly, however, from structure to structure. Decisions purporting to examine only one of these two variables omit a vital step in the analysis. The truth of this proposition is borne out by the Technical Explanations to the 1962 Revenue Act which describe a building in terms of both appearance and function, implying that both criteria must be satisfied before a structure is classed as a "building." The Technical Explanations stated that "building" was to be given its ordinary and commonly understood meaning, save only in the case of the exceptions for storage facilities and structures in the nature of machinery. Does a craneway comport with the common understanding of the term "building"? No. It was erroneously classified as such because the Service refused to examine form, preferring to restrict the analysis to function.

If any sense is to be made of the "building" area, future decisions must take account of the fact that the basic analysis of the section 38 property question should include consideration of all three elements—permanence, form, and function. The corollary to this is that since permanence is assumed in the case of a structure which is arguably a "building,"[362] the consideration should be narrowed to form and function only. The further corollary that in the case of storage facilities function alone is examined is applicable *only* to storage facilities, because there, and only there, can *both* form and permanence be assumed and regarded as constants.

C. The Methodology

A more satisfactory resolution to the chaotic area of "buildings" might proceed as follows. First, both form and function are crucial: no structure which is fundamentally at variance with the common understanding of a building in terms of appearance should be classified as one for the purposes of the investment credit. This would change the whimsical holdings in the instances of the craneway and "clean rooms." If, however, a structure is found to bear the physical earmarks of a building after consideration of its form (and this would include roofless sports arenas that, it is suggested, are gener-

362. This is not always so, of course: if the subject is a trailer then permanence must be examined, as the court properly did in *Joseph H. Moore*, and the Service improperly failed to in Rev. Rul. 67-156, 1967-1 CUM. BULL. 7.

ally thought of as buildings), then the structure should be classified as a "building" unless an analysis of its function demonstrates that it falls within one of four exceptions. The first two exceptions are those provided in the statute for research and storage facilities, which must function as such in connection with certain qualifying activities to be eligible for the credit. The third and fourth exceptions are the "special purpose structure" exemptions now found in the regulations in section 1.48-1(e)(1): structures which are essentially items of machinery, and those which are closely related to property used as an integral part of a qualifying activity.

To dispel prior ambiguities, it should be made clear that structures which are essentially items of machinery should be considered tangible personal property, consistent with *Weirick*'s resolution of the problem with less building-like inherently permanent structures, because of the statement in the regulations that all items in the nature of machinery are tangible personal property.[363] This means that structures coming within this exception are freed from the restrictions of employment only in a qualifying activity, and so need not be used as an integral part of manufacturing, production, etc. It is suggested that since such structures are equipment, allowance of the credit for them regardless of use comports with the policy of the statute.[364] Structures meeting the other, "closely combined with" exception should be considered "other tangible property" since they are by definition less machine-like. Although the Commissioner's present "total dismantling for removal of the property inside" test for this exception should be abandoned as too restrictive, the exception should not be thrown open to all structures containing property used as integral part of manufacturing, etc.: as the regulations presently provide, a structure should meet this exception only on a showing of real interrelationship with the property contained therein. As the regulations state, factors evidencing such a special interrelationship would be peculiar design for the stress and other demands of equipment housed within, and the relative costs of conversion to other uses.

What would the results have been in some of the more recent litigation if this methodology had been applied? *Brown-Forman*'s whiskey sheds would have qualified for the credit, but as storage facilities: it is submitted that the storing while aging of a vast quantity of whiskey in oaken barrels is the bulk storage of a fungible

363. Treas. Reg. § 1.48-1(c) (1975).

364. For example, even if the nation's industrial base is not boosted by the employment of this property in fabricating industries, those industries nevertheless receive a tonic by virtue of manufacturing this property.

commodity. But *Brown-Forman*'s statements that the sheds are not buildings should be repudiated: they *are* buildings, but are permitted the credit because they are a special class of buildings. The *Satrum* henhouses, however, present a different case. Certainly, the henhouses passed the appearance test: they *looked* like buildings. To qualify for the credit, they must then meet one of the four exceptions. They are pretty clearly neither research nor storage facilities. It seems fanciful to argue that they are machinery. They must qualify or not, then, on the closeness of their relation to the property contained inside. Although the Tax Court made some rather questionable observations about the primacy of function over all other considerations, it seems to have been on the right track in concluding "there is little doubt in our mind that the structure was specially designed as an integral part of the egg-producing process."[365] The court discussed at some length the peculiar features of the structure, such as louvered walls and sloping floor for easy washing and drainage; the court observed further that the henhouse could not be used for any purpose except for the quartering of chickens, and noted that replacement of the entire facility reasonably could be expected if the property housed inside were abandoned. The difficulty with the case is that one suspects that the court has overstated the importance of the interrelationship between the henhouse and the egg process: was this henhouse really any more closely and inextricably related to property used as an integral part of manufacturing or production than were the greenhouses in *Sunnyside* and *Thirup*? The Senate Report on which this exception is based refers to an automated hog-raising facility, describing it in such terms that one receives the impression of a robot hog-raising machine. The Tax Court felt that the henhouse was of similar character. It is suggested that if this henhouse is indeed within this exception, it is only barely within it. A much more convincing example would be the beer cellars in *Adolph Coors*, literally crammed with brewing equipment and heavy insulation functioning as indispensible parts of the brewing process. But while we may have some doubts about a factual judgment call made in a close case, the Tax Court's methodology in *Satrum* may well stand as a harbinger of a recognition that form, function, and permanence must be considered together in any section 38 property question.

Twelve full years have elapsed since section 38 property made its first appearance on the stage of tax law. In those twelve years, a complicated, confusing, ad hoc, and often inconsistent body of rul-

365. CCH TAX CT. REP. ¶ 32,665 at 2755 (1974).

ings and judicial decisions has grown up around the definitional regulation; words and phrases have acquired strange new meanings and connotations in the lush overgrowth of legal reasoning clinging to that regulation. The paradoxes in the regulation (such as that addressed in *Weirick*) and, more often, the ambiguities resulting from an almost universal failure by the regulations to define, instead of simply *illustrate*, its terms (such as "inherently permanent structure," "structural component," "building," and the rest) perhaps make inconsistency in and confusion over interpretation inevitable. Nevertheless, it is submitted that the practitioner, the Service, and the courts could bring some order into the chaos of section 38 property by developing and consistently applying a single methodology of analysis, such as the tripartite consideration of form, function, and permanence suggested herein, which would provide an underlying foundation of logic and common sense for the area in which such a foundation heretofore has been sorely missed.

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