

Internal Revenue Service**Department of the Treasury**

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Washington, DC 20224

Person to Contact:

Telephone Number:
(202) 622-4920

Refer Reply To:
CC:ITA:4 – PLR-167260-01

Date: April 9, 2002

Re:

LEGEND:

X =

Dear

This letter is in response to your letter dated December 6, 2001, requesting a ruling that you may include your share of the costs of a shoreline stabilization project in the adjusted basis of X, the residence that you sold in March 2001.

You state the facts as follows. X is situated on a bluff of land overlooking a river. After your purchase of X, you became aware that the bluff was eroding and that X was at risk. An engineering firm recommended the construction of a new bulkhead and reconstruction of the bluff. As the proposed construction site of the bulkhead and much of the bluff were on “commons” land for which no one had title to or responsibility for, you obtained the necessary permits for the construction from the county and the state. After completion of the project, the state inspected and approved the construction. In March 2001, you sold X.

Section 1016 of the Internal Revenue Code provides that the basis of property shall be adjusted for capital expenditures. Section 1.1016-2 of the Income Tax Regulations provides that the basis of property shall be adjusted for any expenditure properly chargeable to capital account, including the cost of improvements and betterments made to the property.

In Red Star Yeast and Products Co. v. Commissioner, 25 T.C. 321 (1955), the taxpayer’s manufacturing plant was built on a bluff overlooking Lake Michigan. In response to the erosion of the bluff on which the plant was located, the taxpayer obtained a permit from the War Department to build jetties in the lake opposite its property. The taxpayer then built two jetties to protect its property and sought to deduct construction costs. The court held, agreeing with the Commissioner’s position, that the construction costs of the jetties were capital expenditures.

Similarly, in Rev. Rul 60-386, 1960-2 C.B. 107, a taxpayer owned a tract of land along the western coast of the United States. The taxpayer became aware that the land was subsiding, and in response constructed sea walls, related bulkheads, and drainage systems. The construction represented entirely new assets and a complete substitution of structures, utilizing different materials, which adapted the property to changed surroundings and provided protection from future damage. The revenue ruling concludes that the taxpayer’s expenditures were capital expenditures.

Whether an expenditure is capital in nature depends on the facts of the case. Here, the facts show that the project improved and bettered X by stabilizing the shoreline and protecting X from future damage. Therefore, the costs of the construction of the new bulkhead and the reconstruction of the bluff are capital in nature. Accordingly, we conclude that you may add these costs to the adjusted basis of X for purposes of determining your gain on its sale.

CAVEATS:

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose a copy of the letter for this purpose. Also enclosed is a copy of the letter ruling showing the deletions proposed to be made in the letter when it is disclosed under §6110.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any item discussed or referenced in this letter. This ruling is directed only to the taxpayers requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Robert A. Berkovsky
Branch Chief
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosures (2)