OFFICE OF
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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MEMORANDUM FOR Industry Director, Natural Resources & Construction
(LM:NRC)

FROM: Branch Chief, Branch 6, Office of Associate Chief Counsel
(Passthroughs & Special Industries)
(CC:PSI:6)

SUBJECT: Withdrawal of Application for Change in Method of Accounting

In accordance with section 8.07(2)(a) of Rev. Proc. 2002-1, 2002-1 I.R.B. 1, 34, this Chief Counsel Advice advises you that a taxpayer within your division has withdrawn its Form 3115, Application for Change in Accounting Method. Pursuant to § 6110(k)(3) of the Internal Revenue Code, this Chief Counsel Advice may not be used or cited as precedent.

LEGEND:

B =

C =

D =

E =

F =

x =

y =

This Chief Counsel Advice advises you that a Form 3115, dated C, filed on behalf of B, is withdrawn. B did not give any reason for the withdrawal.

B had requested to change its method of determining salvage value for depreciable assets described in asset class 49.14, Electric Utility Transmission and Distribution

Facilities, of Rev. Proc. 72-10, 1972-1 C.B. 721 (and its successors) that were placed in service from 1971 through 1980 and depreciated under the Class Life Asset Depreciation Range system (CLADR) provided in § 1.167(a)-11 of the Income Tax Regulations. Hereinafter, these assets are referred to as T&D assets. Presently, B estimated the salvage value of these T&D assets to be x percent, by taking a six-year average of salvage realized or recognized on property retired during the six years before 1971. B did not update this estimate for each succeeding taxable year. B proposes to use a salvage value of y percent for the T&D assets at issue, which B states is the estimate used by the utility industry. This change would have been effective beginning with the taxable year beginning D.

At the time of the withdrawal, B had been advised of our tentatively adverse position and had been granted a conference of right on E, to discuss its proposed change.

We are tentatively adverse to B's proposed change for the following reasons:

1. B had elected CLADR for its eligible property placed in service from 1971 through 1980. Accordingly, B has consented to, and agreed to apply, all the provisions of § 1.167(a)-11 for these assets. Section 1.167(a)-11(a)(1).

Section 1.167(a)-11(d)(1) prescribes the rules for salvage value under the elective CLADR. The term "salvage value" is defined in § 1.167(a)-11(d)(1)(ii) as meaning gross salvage value (as defined in § 1.167(a)-11(d)(1)(i)) less the amount, if any, by which the gross salvage value is reduced by application of § 167(f) of the Internal Revenue Code of 1954. Section 1.167(a)-11(d)(1)(iii) provides that the salvage value of each vintage account of the taxable year shall be estimated by the taxpayer at the time the election to apply CLADR is made, upon the basis of all facts and circumstances existing at the close of the taxable year in which the account is established.

For CLADR elections, § 1.167(a)-11(d)(1)(v) provides that the salvage value established by the taxpayer for a vintage account will not be redetermined if it is reasonable. This regulation further provides that the salvage value established by the taxpayer will be deemed to be reasonable unless there is sufficient basis in the facts and circumstances existing at the close of the taxable year in which the account is established for a determination of an amount of salvage value for the account that exceeds the salvage value established by the taxpayer for the account by an amount greater than 10 percent of the unadjusted basis of the account at the close of the taxable year in which the account is established. Section 1.167(a)-11(d)(1)(v) also provides that a determination of salvage value shall include all determinations at all levels of audit and appellate proceedings, and as well as all final determinations within the meaning of § 1313(a)(1).

In the present case, B determined the salvage value for the vintage accounts for the T&D assets at issue to be x percent and now proposes to change to a salvage value that is less than x percent. Accordingly, pursuant to § 1.167(a)-11(d)(1)(v), the salvage value of x percent originally established by B is deemed to be reasonable and, therefore, should not be redetermined.

2. B proposes to use a salvage value of y percent, which B states is the estimate used by the utility industry. In establishing salvage value estimates, general industry experience may be used until the taxpayer has adequate experience upon which to base the estimate. B, however, had adequate experience to base its estimate of salvage value and, therefore, general industry experience is unacceptable in this case. In its letter dated F, B stated that it is in the process of developing an estimate of salvage based upon the facts and circumstances that existed as of the close of the taxable year for each year in which the CLADR election was made. At the time of the withdrawal, B had not submitted those estimates to us.

We note that to the extent that B sells or otherwise disposes of assets retired to a materials and supplies account or a construction work-in-process account, those facts must be reflected in estimating salvage value.

If you have any questions on this matter, do not hesitate to call (202) 622-3110.

Charles B. Ramsey
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