Internal Revenue Service

Number: **202519002**
Release Date: 5/9/2025

Index Number: 168.24-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:ECE:B02
PLR-112035-24

Date:
February 03, 2025

Re:

LEGEND:

Taxpayer	=
Parent	=
Manufacturer	=
Commission A	=
Commission B	=
Commission C	=
Commission D	=
State A	=
State B	=
State C	=
a	=
b	=
c	=
d	=
e	=
Date A	=
Date B	=
Order	=

Dear :

This letter responds to your request, received July 3, 2024, for a ruling regarding certain federal income tax consequences under § 168(i)(10) and former § 46(f) of the Internal

Revenue Code of the proposed transactions described below. The relevant facts as represented in your submission are set forth below.

FACTS

Taxpayer is wholly owned by Parent, a State A corporation, and is considered a division of Parent. Parent is the common parent of an affiliated group of corporations that file a consolidated federal income tax return on a calendar year basis using the accrual method of accounting.

Taxpayer is a regulated public utility primarily engaged in the generation, transmission, distribution, and sale of electricity in portions of State B and State C, and its service area covers approximately a square miles and supplies electric serves to b residential, commercial, and industrial customers. Taxpayer is subject to the regulatory provisions of Commission A, Commission B, Commission C, and Commission D.

Manufacturer and Taxpayer have negotiated a Renewable Energy Procurement and Service Agreement (Enabling Agreement) for the provision of renewable energy from Taxpayer to Manufacturer's State C based facility. The Enabling Agree, which was entered into by both parties on Date A and approved by Commission B on Date B, allows Taxpayer to serve Manufacturer under a special retail arrangement whereby Taxpayer and Manufacturer shall enter into project-specific power purchase agreements (PPA) negotiated at a later date to virtually and physically serve Manufacturer's load within Taxpayer's territory. These PPAs would include the following projects:

1) A c year agreement for d MW-AC grid-scale renewable energy projects, referred to herein as "Project A";
2) A c year agreement for e MW-AC rooftop systems to be installed on one or more of Manufacturer's buildings, referred to herein as "Project B".

Enabling Agreement

The Enabling Agreement establishes the structure for the special arrangements, separate and apart from existing Commission B approved tariffs and rate schedules, whereby Manufacturer may purchase power and renewable energy credits from Taxpayer under the project agreements described at bilaterally negotiated rates, terms and conditions.

Project A

Under the Enabling Agreement, Taxpayer would own, operate, and maintain the renewable facility, and would file the final agreement, including negotiated pricing, with Commission B as a special contract. The solar asset would not be included in Taxpayer's rate-base with Commission B.

The proposed structure is a utility-scale virtual power purchase agreement (PPA) where Taxpayer will charge Manufacturer $/MWh rate to be negotiated between the parties under the PPA, subject to approval by Commission B. All of the energy and associated renewable energy credits produced by Project A over the term of the agreement will be sold to Manufacturer under the terms of the PPA.

Under the virtual PPA, the transaction will be exclusively financial, as no energy will be physically directly delivered to Manufacturer, but rather simply to Commission B's gird at the point of interconnection. Manufacturer will be credited with the relative value of the energy delivered to the grid based on a valuation formula to be negotiated by the parties. Taxpayer will also maintain separate accounting records for these transactions contemplated in the Enabling Agree so that no incremental costs associated with it or the PPA will be included in Taxpayer's rate base or cost of service used to calculate rates for Taxpayer's Commission B customers.

Project B

The rooftop system developed under Project B would be electrically connected on Manufacturer's side of the regulated retail service interconnection and metering point and would not deliver any energy back to the grid. Similar to Project A, under the proposed agreement, Taxpayer would own, operate, and maintain the renewable facility, and would file the final agreement, including negotiated pricing, with Commission B as a special contract. The solar asset would not be included in Taxpayers rate-base with Commission B.

RULINGS REQUESTED

Taxpayer requested the following rulings:

(1) Project A will not be public utility property within the meaning of former § 46(f) (of continuing applicability by virtue § 50(d)(2), § 168(i)(10) and the regulations promulgated thereunder.

(2) Project B will not be public utility property within the meaning of former § 46(f) (of continuing applicability by virtue § 50(d)(2), § 168(i)(10) and the regulations promulgated thereunder.

LAW AND ANALYSIS

Section 168(f)(2) provides that the depreciation deduction determined under § 168 shall not apply to any public utility property (within the meaning of § 168(i)(10)) if the taxpayer does not use a normalization method of accounting.

Section 168(i)(10) defines, in part, public utility property as property used predominantly in the trade or business of the furnishing or sale of electrical energy if the rates for such

furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

Prior to the Revenue Reconciliation Act of 1990, § 168(i)(10) defined public utility property by means of a cross reference to § 167(l)(3)(A). Section 167(l)(3)(A) as then in effect contained the same definition of public utility property that is currently in § 168(i)(10). Section 1.167(l)-1(b) provides that under § 167(l)(3)(A), property is public utility property during any period in which it is used predominantly in a § 167(l) public utility activity. The term "section 167(l) public utility activity" means, in part, the trade or business of the furnishing or sale of electrical energy if the rates for such furnishing or sale, as the case may be, are regulated, i.e., have been established or approved by a regulatory body described in § 167(l)(3)(A). The term "regulatory body described in section 167(l)(3)(A)" means a State (including the District of Columbia) or political subdivision thereof, any agency or instrumentality of the United States, or a public service or public utility commission or other body of any State or political subdivision thereof similar to such a commission. The term "established or approved" includes the filing of a schedule of rates with a regulatory body which has the power to approve such rates, though such body has taken no action on the filed schedule or generally leaves undisturbed rates filed by the taxpayer.

The definitions of public utility property contained in § 168(i)(10) and former § 46(f)(5) are essentially identical. Pursuant to § 50(d)(2), rules similar to the rules of former § 46(f), as in effect on November 5, 1990, continue to determine whether an asset is public utility property for purposes of the investment tax credit normalization rules. As in effect at that time, former § 46(f)(5) defined public utility property by reference to former § 46(c)(3)(B).

The regulations under former § 46 (of continuing applicability by virtue of § 50(d)(2)), specifically § 1.46-3(g)(2)(iii), contains an expanded definition of regulated rates. This expanded definition embodies the notion of rates established or approved on a rate of return basis; where rate of return includes a fair return on the taxpayer’s investment in providing such goods and services. Furthermore, rates are not “regulated” if they are established or approved on the basis of maintaining competition within an industry, insuring adequate service to customers of an industry, or charging “reasonable” rates within an industry. In addition to the definition in the § 46 regulations, there is an expressed reference to rate of return in § 1.167(l)-1(h)(6)(i).

The operative rules for normalizing timing differences relating to use of different methods and periods of depreciation are only logical in the context of rate-of-return regulation. The normalization method, which must be used for public utility property to be eligible for the depreciation allowance available under § 168, is defined in terms of the method the taxpayer uses in computing its tax expense for purposes of establishing its cost of service for ratemaking purposes and reflecting operating results in its

regulated books of account. Therefore, for purposes of application of the normalization rules, the definition of public utility property is the same for purposes of the investment tax credit and depreciation.

Thus, under both the depreciation and investment tax credit normalization rule definitions, a facility must meet three requirements to be considered public utility property:

(1) It must be used predominantly in the trade or business of the furnishing or sale of, inter alia, electrical energy;

(2) The rates for such furnishing or sale must be established or approved by a State or political subdivision thereof, any agency or instrumentality of the United States, or by a public service or public utility commission or similar body of any State or political subdivision thereof; and

(3) The rates so established or approved must be determined on a rate-of-return basis.

Taxpayer will predominantly use Project A and Project B in the trade or business of the furnishing or sale of electric energy. Therefore, Project A and Project B will meet the first requirement. In addition, Taxpayer is a regulated public utility company subject to the jurisdiction of federal and state law, including the ratemaking jurisdiction of Commission A, B, C, D. Therefore, Project A and Project B will also meet the second requirement.

However, as described above, the rates Taxpayer charges for electricity to be produced by Project A and Project B will be the rates negotiated by Taxpayer and Manufacturer. These rates will be the only source of compensation to Taxpayer for electricity produced by Project A and Project B; and none of the costs associated with Project A or Project B will be included in Taxpayer rate-base for Commission B. Thus, the rate for Project A and Project B cannot be characterized as rate-of-return price setting. Therefore, Project A and Project B will not meet the third requirement.

Accordingly, we conclude that:

(1) Project A will not be public utility property within the meaning of former § 46(f) (of continuing applicability by virtue of § 50(d)(2), § 168(i)(10) and the regulations promulgated thereunder.

(2) Project B will not be public utility property within the meaning of former § 46(f) (of continuing applicability by virtue § 50(d)(2), § 168(i)(10) and the regulations promulgated thereunder.

We have given these rulings requested above based on the representations of the Taxpayer and the conclusions of Commission B as described above. While the Enabling Agreement was signed and entered into by both parties, the final agreements on the price to be paid for electricity, the final details of Project A and Project B, and the approval by Commission B were not presented as part of this ruling request. These rulings are contingent upon the final versions of these agreements being substantially in accord with the representations herein and Commission B's Order dated Date B.

Except as specifically determined above, no opinion is expressed or implied concerning the Federal income tax consequences of the matters described above under any other provisions of the Code (including other subsections of § 168). In addition, no opinion is expressed concerning whether Taxpayer is the owner of the facilities generating electricity for federal income tax purposes.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent. This ruling is based upon information and representations submitted by Taxpayer and accompanied by penalty of perjury statements executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for a ruling, it is subject to verification on examination.

This letter is being issued electronically in accordance with Rev. Proc. 2020-29, 2020-21 I.R.B. 859. A paper copy will not be mailed to Taxpayer.

In accordance with the power of attorney on file with this office, we are sending a copy of this letter to your authorized representative. We are also sending a copy of this letter to the LB&I Policy Office.

Sincerely,

Patrick S. Kirwan
Chief, Branch 2
Office of the Associate Chief Counsel
(Energy, Credits, & Excise)

Enclosure:
Copy for § 6110 purposes
cc:

LB&I Policy Office