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Date:
July 28, 2005

Legend:

Seller =

Buyer =

Plant =
Location =
State =
Seller's Parent =
Intermediate =
Buyer's Parent =
Agency =
Commission A =
Commission B =
Trustee =
System Operator =
New Rule =
Order One =
Order Two =

a =
b =
c =
d =
e =
f =
g =
h =

i =
j =
k =

Dear

This letter responds to a letter, dated October 29, 2004, requesting a private letter ruling concerning the tax consequences of the sale of an interest in a nuclear power plant and associated assets and liabilities, including nuclear decommissioning liability, between Seller and Buyer. Specifically, you have requested rulings regarding the tax consequences, under section 468A of the Internal Revenue Code, to Seller's nuclear decommissioning funds and Buyer's nuclear decommissioning funds, as well as rulings regarding the proper realization and recognition of gain and loss on the sale of Seller's interest in the nuclear power plant and associated assets.

Seller and Buyer, in a jointly-filed ruling request, have represented the following facts and information relating to the ruling request:

Plant is located in Location, in State, and consists of two units and associated assets located together on a single property.

Seller, a regulated public utility company, is a wholly-owned subsidiary of Seller's Parent, a public utility holding company that, directly or indirectly, owns several regulated and unregulated energy companies. Seller is a member of Seller's Parent's affiliated group and joins in filing a consolidated return on a calendar year basis using the accrual method of accounting. Seller and Seller's Parent are under the audit jurisdiction of the Immediately prior to the transfer of the Plant to Buyer, Seller owns a a percent undivided ownership interest in the Plant. Simultaneous with execution of the transaction discussed in this ruling letter, taxpayer will transfer a b percent interest in the Plant to Agency, a party unrelated to both Seller and Buyer. This letter ruling, therefore, relates only to the transfer of Seller's remaining c percent interest in Plant.

Prior to the transfer of the Plant to Buyer, Seller's wholesale electric power sales are subject to the jurisdiction of Commissions A and B. Pursuant to a trust agreement with Trustee, Seller has established, with respect to the decommissioning of its interest in Plant, a nuclear decommissioning fund qualifying under section 468A, and a nuclear decommissioning fund that does not meet the requirements of section 468A, for each unit of Plant. The level of funding in the nuclear decommissioning funds is based on estimates of the future costs that the owner of the Plant will incur upon the decommissioning of the Plant.

Buyer, a limited partnership, is wholly-owned by two entities that are in turn wholly-owned by Intermediate, a corporation. The taxpayers represent that Buyer and

these intervening entities are disregarded entities for federal tax purposes, and that as a consequence Buyer is treated as a division of Intermediate. Buyer's Parent, a publicly-owned holding company with energy-related subsidiaries, holds d percent of the common stock of Intermediate through a disregarded entity. The remaining e percent of the common stock of Buyer is publicly-traded. Buyer's Parent and its subsidiaries, including Buyer, file a consolidated return on a calendar year basis using the accrual method of accounting. Buyer and Buyer's Parent are under the audit jurisdiction of the

Buyer currently owns a f percent undivided interest as a tenant in common in the Plant. Buyer's operations are subject to the protocols of System Operator, the independent system operator for the applicable power region under substantive rules promulgated by Commission A. Pursuant to a trust agreement with Trustee, Buyer has established, with respect to the decommissioning of its existing f percent interest in Plant, a nuclear decommissioning fund qualifying under section 468A, and a nuclear decommissioning fund that does not meet the requirements of section 468A, for each unit of Plant.

On g, Buyer (and Agency) entered into the Purchase and Sale Agreement ("PSA") with Seller. Under the PSA, Seller is obligated to transfer to Buyer at the closing of the transaction Seller's undivided c percent interest in Plant, including a proportionate amount of the assets constituting or necessary to operate the Plant and a proportionate amount of the assets of the qualified and nonqualified nuclear decommissioning funds maintained by Seller with respect to its interest in the Plant in exchange for Buyer's payment of an initial price of $h in cash (subject to various adjustments) and Buyer's assumption of certain liabilities and obligations of Seller, including a proportionate amount of Seller's liability and obligation to decommission the Plant. The transferred assets of Seller's qualified and nonqualified decommissioning funds will be held by Trustee in qualified and nonqualified decommissioning funds established by Buyer for each unit of Plant. The Commission A orders establishing rates to be charged to ratepayers with respect to Buyer's c percent interest in Plant will be separate from the Commission A orders establishing the rates charged to ratepayers with respect to Buyer's f percent interest in Plant. The corpus and income of Buyer's qualified and nonqualified decommissioning funds will be held for decommissioning each respective unit of the Plant. Once decommissioning begins, expenses will be paid directly by the qualified and nonqualified decommissioning funds for each unit of Plant.

The PSA requires Buyer to complete, at its expense, the complete retirement and removal from service of the acquired interest in the Plant, including any necessary site restoration. Following the transfer of Seller's c percent interest the Plant to Buyer, Buyer will own, in total, a i percent interest in the Plant. After the sales to Buyer and Agency, Seller will no longer be engaged in the trade or business of nuclear generation at the Plant or any other nuclear facility.

Seller and Buyer represent that they will treat the transaction as an asset purchase for tax purposes, subject to section 1060 of the Code, and will agree to an allocation of the Purchase Price among the Purchased Assets (excluding the assets comprising the qualified nuclear decommissioning funds for each unit of Plant) that is consistent with the allocation methodology provided by sections 1060 and 338 and the regulations thereunder.

Buyer has established and will maintain qualified and nonqualified nuclear decommissioning funds for each unit of Plant to satisfy Buyer's liability to decommission the c percent interest in the Plant acquired from Seller. Buyer interprets Commission A's New Rule as requiring Buyer to maintain these trusts separate and apart from the nuclear decommissioning funds it maintains for its existing interest in the Plant. The New Rule also provides that these nuclear decommissioning funds will be subject to regulation by Commission A. With respect to each unit of the Plant, Buyer intends to treat the existing qualified nuclear decommissioning fund for that unit and the qualified nuclear decommissioning fund for the acquired c percent interest in that unit of the Plant as a single qualified nuclear decommissioning fund for purposes of section 468A, even though the funds are maintained by separate trusts.

On j, in Order One, Commission A authorized Seller to continue collecting nuclear decommissioning costs in a nonbypassable charge to retail customers (the "Decommissioning Collections"). Seller has collected, and continues to collect, decommissioning costs through such a nonbypassable charge from its retail electric customers.

After the sale, Seller will continue to collect the Decommissioning Collections on behalf of, and for the benefit of, Buyer, in accordance with the New Rule and pursuant to a Decommissioning Funds Collection Agreement to be entered into by the parties. The agreement will provide rules applicable to the period after the closing pertaining to Buyer's administration of the nuclear decommissioning funds for each unit of Plant, the collection of decommissioning revenues from Seller's retail electric customers by Seller as an agent for Buyer, and the weekly remittance by Seller of the collected revenues to the nuclear decommissioning funds maintained by Buyer. In Order Two, dated k, Commission A clarified that the Decommissioning Collections charged to Seller's retail electric customers is collected for the benefit of the owner of the interest in the Plant (i.e. Buyer), and that such owner is required to contribute the collections to its nuclear decommissioning funds.

State enacted the New Rule to ensure that adequate funds will be available to decommission nuclear power plant that have been transferred out of State-jurisdictional rate base. The New Rule provides that, following the transfer of a State-jurisdictional nuclear power plant and the associated nuclear decommissioning funds, any remaining costs associated with nuclear decommissioning obligations will remain subject to cost of service regulation based upon a periodic review of the costs. Under the New Rule, Seller and Taxpayer are required to enter into a Decommissioning Funds Collection

Agreement that governs the transfer of responsibility for the administration of the nuclear decommissioning funds, the collection of decommissioning revenues from utility customers, and the remittance of the funds to the nuclear decommissioning funds. The New Rule requires that the parties submit the Decommissioning Funds Collection Agreement and any subsequent amendments to Commission A for approval. The New Rule also requires that Taxpayer periodically perform a study of the cost of decommissioning Plant, and to submit the study along with an updated analysis of decommissioning costs to Commission A. Taxpayer is required to demonstrate to Commission A that the funds are being invested prudently and in compliance with the New Rule, and that Taxpayer is making efforts to achieve optimum tax efficiency with respect to the nuclear decommissioning funds. Commission A or any affected person may initiate a proceeding to review the balance of the funds, compliance with the New Rule, or the annual funding amount. Taxpayer must file an annual report of the status of the funds with Commission A.

The New Rule requires that if a taxpayer has an existing trust for the same generating unit in which an interest is being transferred that is funded by a set of ratepayers entirely distinct from the transferor's ratepayers, a separate trust or subaccount shall be maintained that will segregate the decommissioning funds received from the transferor, and the earnings thereon, from the nuclear decommissioning trust funds received from other sources.

The taxpayers represent that Buyer will be a named recipient of, and will be bound by the terms of, all orders issued by Commission establishing the cost of decommissioning Buyer's interest in Plant and establishing the amount to be collected from ratepayers with respect to that cost.

Commission A intends to issue a separate order to Buyer specifying the fixed annual funding amount approved by Commission A as Buyer's cost of service for decommissioning its c percent interest in the Plant. Commission A will periodically review this amount and, when necessary, issue orders to Buyer adjusting such amount. Buyer may also initiate proceedings for Commission A review and adjustment of this amount.

Requested Ruling #1: *The transfer of a proportionate amount of the assets from Seller's qualified nuclear decommissioning funds to Buyer's qualified nuclear decommissioning funds is a disposition that satisfies the requirements of section 1.468A-6(b) and, accordingly, each of Buyer's qualified nuclear decommissioning funds, which will hold a proportionate amount of the assets in Seller's qualified nuclear decommissioning funds, will be treated as a qualified nuclear decommissioning fund that satisfies the requirements of section 468A and the regulations thereunder.*

Section 468A(a) of the Code provides that a taxpayer may elect to deduct payments made to a qualified nuclear decommissioning reserve fund. Section 468A(b) limits the annual deduction of the electing taxpayer to the lesser of the ruling amount or

the amount of decommissioning costs included in the electing taxpayer's cost of service for ratemaking purposes for the taxable year. Section 468A(e)(4) provides, in pertinent part, that the assets in a qualified fund shall be used exclusively for satisfying the liability of any taxpayer contributing to the qualified fund.

Section 1.468A-5(a) of the Federal Income Tax Regulations sets out the qualification requirements for nuclear decommissioning funds. It provides, in part, that a qualified fund must be established and maintained pursuant to an arrangement that qualifies as a trust under state law. An electing taxpayer can establish and maintain only one qualified fund for each nuclear power plant. Section 1.468A-5(c)(1)(i) provides that if, at any time during the taxable year, a nuclear decommissioning fund does not satisfy the requirements of section 1.468A-5(a) the Service may disqualify all or a portion of the fund as of the date that the fund does not satisfy the requirements. Section 1.468A-5(c)(3) provides that if a qualified fund is disqualified the fair market value (with certain adjustments) of the assets in the fund is deemed to be distributed to the electing taxpayer and included in that taxpayer's gross income for the taxable year.

Section 1.468A-6 generally provides rules for the transfer of an interest in a nuclear power plant (and transfer of the qualified fund) where after the transfer the transferee is an eligible taxpayer. Under section 1.468A-6(g), the Service may treat any disposition of an interest in a nuclear power plant occurring after December 27, 1994, as satisfying the requirements of the regulations if the Service determines that such treatment is necessary or appropriate to carry out the purposes of section 468A.

Under the specific facts herein, the Service will exercise its discretion to treat this transaction, under section 1.468A-6(g), as a disposition qualifying under the general provisions of section 1.468A-6. This exercise of discretion, however, applies to the provisions of section 1.468A-6 except those outlined in section 1.468A-6(e) with respect to the calculation of a schedule of ruling amounts subsequent to a sale. Thus, under section 1.468A-6 Seller's qualified nuclear decommissioning funds for each unit of Plant will not be disqualified upon the transfer of the assets of those funds to Buyer's qualified nuclear decommissioning funds for each unit of Plant, and Buyer's qualified nuclear decommissioning funds will be treated as qualified nuclear decommissioning funds as defined in section 468A.

Requested Ruling #2: *Neither Buyer nor Buyer's qualified nuclear decommissioning funds will recognize any gain or loss or otherwise take any income or deduction into account by reason of the transfer of a proportionate amount of the assets of Seller's qualified nuclear decommissioning funds to Buyer's qualified nuclear decommissioning funds, and Buyer's qualified nuclear decommissioning funds will have a carryover basis in the assets received from Seller's qualified nuclear decommissioning funds.*

Section 1.468A-6(c)(2) provides that neither a transferee nor its fund will recognize gain or loss or otherwise take any income or deduction into account by reason of the transfer of the assets from a transferor's qualified fund to a transferee's

qualified fund. Thus, neither Buyer nor Buyer's qualified nuclear decommissioning funds will recognize gain or loss or otherwise take any income or deduction into account by reason of the transfer of the assets of Seller's qualified nuclear decommissioning funds to Buyer's qualified nuclear decommissioning funds.

Section 1.468A-6(c)(3) provides that transfers of assets of a qualified nuclear decommissioning fund to which section1.468A-6 applies do not affect basis. Thus, Buyer's qualified nuclear decommissioning funds will have a basis in the assets received from Seller's qualified nuclear decommissioning funds that is the same as the basis of those assets in Seller's funds immediately before the date of transfer.

Requested Ruling #3: *Neither Seller nor Seller's qualified nuclear decommissioning funds will recognize any gain or loss or otherwise take any income or deduction into account upon the transfer of a proportionate amount of the assets of Seller's qualified nuclear decommissioning funds to Buyer's qualified nuclear decommissioning funds.*

Section 1.468A-6(c)(1) provides that neither a transferor nor its fund will recognize gain or loss or otherwise take any income or deduction into account by reason of the transfer of the assets from a transferor's qualified fund to a transferee's qualified fund. Thus, neither Seller nor the qualified nuclear decommissioning funds maintained by Seller for Plant will recognize gain or loss or otherwise take any income or deduction into account by reason of the transfer of the qualified nuclear decommissioning fund assets to Buyer's qualified nuclear decommissioning funds.

Requested Ruling #4: *With respect to each unit of the Plant, the qualified nuclear decommissioning fund maintained under Buyer's New Decommissioning Trust Agreement and the qualified nuclear decommissioning fund maintained under Buyer's Existing Decommissioning Trust Agreement will be treated as a single qualified nuclear decommissioning fund for purposes of section 468A. Accordingly, the maintenance of the separate funds will not disqualify Buyer's qualified nuclear decommissioning funds.*

Section 1.468A-5(a)(iii) provides that an electing taxpayer can establish and maintain only one qualified fund for each nuclear power plant. If a nuclear plant is subject to the ratemaking jurisdiction of two or more public utility commissions and any such public utility commission requires a separate fund to be maintained for the benefit of ratepayers whose rates are established or approved by the public utility commission, the separate fund maintained for such plant (whether or not established and maintained pursuant to a single trust agreement) shall be considered a single nuclear decommissioning fund for purposes of section 468A and sections 1-468A-1 through 1.468A-5, 1.468A-7, and 1.468A-8 of the regulations.

Under section 1.468A-6(g), the Service may treat any disposition of an interest in a nuclear power plant occurring after December 27, 1994, as satisfying the requirements of the regulations if the Service determines that such treatment is necessary or appropriate to carry out the purposes of section 468A.

Taxpayer does not meet the literal requirements of section 1.468A-5(a)(iii) because it maintains more than one qualified nuclear decommissioning fund for each unit of the Plant (one fund for the existing interest in each unit, and one fund for the interest in each unit acquired from Seller), established pursuant to separate trust documents under the jurisdiction of one public utility commission rather than multiple public utility commissions. However, the facts submitted by Seller and Buyer state that Commission A requires that the assets of the qualified nuclear decommissioning fund maintained for each unit of the Plant under Buyer's New Decommissioning Trust Agreement not be commingled with the assets of the qualified nuclear decommissioning fund maintained for that unit under Buyer's Existing Decommissioning Trust Agreement. In addition, Commission A issues two separate rate orders to Buyer, one for the qualified nuclear decommissioning funds maintained under the New Decommissioning Trust Agreement and the other for the qualified nuclear decommissioning funds maintained under the Existing Decommissioning Trust Agreement.

In order to permit Buyer to comply with New Rule and Commission A's order, we are exercising our discretion under section 1.468A-6 to approve the disposition of Plant and the associated nuclear decommissioning funds. We will treat the two separate rate orders issued by Commission A approving decommissioning costs for Buyer's two separate interests in Plant as having been issued by two separate commissions for purposes of section 1.468A-5(a)(iii). Accordingly, we conclude that Buyer may maintain separate qualified nuclear decommissioning funds for these interests in Plant, and the maintenance of the separate funds will not disqualify Buyer's qualified nuclear decommissioning funds. This exercise of discretion is valid only so long as the New Rule is in effect, and only so long as Commission A requires separate qualified nuclear decommissioning funds to be maintained.

Requested Ruling #5: *Seller's gain or loss on the sale of a proportionate amount of the Purchased Assets (excluding Seller's qualified nuclear decommissioning funds) to Buyer will equal the difference between a proportionate amount of Seller's tax basis in each asset and the amount realized with respect to that asset, taking into account the allocation of consideration pursuant to section 1060 and the regulations thereunder. Seller's amount realized from the sale of a proportionate amount of the Purchased Assets (excluding Seller's qualified nuclear decommissioning funds) will include the cash received from Buyer and a proportionate amount of the liability to decommission the Plant (reduced by the amount of the decommissioning liability to be funded by the qualified nuclear decommissioning funds), to the extent such liabilities and obligations are taken into account as liabilities for federal income tax purposes.*

Section 1001(a) provides that gain from the sale of property shall be the excess of the amount realized over the adjusted basis provided in section 1011 for determining gain, and that loss from the sale of property shall be the excess of the adjusted basis provided in section 1011 for determining loss over the amount realized. Section 1001(b) provides that a seller’s amount realized from the sale of property is the sum of

any money received plus the fair market value of the property (other than money) received.

Section 1.1001-2(a)(1) of the Income Tax Regulations provides that a seller's amount realized from the sale of property includes the amount of liabilities from which the seller is discharged as a result of the sale. They may include debt and non-debt liabilities. Fisher Co. v. Commissioner, 84 T.C. 1319, 1345-47 (l985) (assumption of lessee's repair liability was part of amount realized on sale of leasehold). The decommissioning liability from which Seller will be relieved is fixed and determinable. As an owner and operator of the Plant, Seller is required by law to provide for eventual decommissioning.

Section 1060 provides that, in the case of an applicable asset acquisition, the consideration received for such assets shall be allocated among the acquired assets in the same manner as amounts are allocated to assets under section 338(b)(5). Section 1.1060-1(a)(1) provides that, in the case of an applicable asset acquisition, sellers and purchasers must allocate the consideration under the residual method as described in sections 1.338-6 and 1.338-7 in order to determine, respectively, the amount realized from, and the basis in, each of the transferred assets.

Section 1060(c) defines the term applicable asset acquisition as the transfer of assets constituting a trade or business if the acquirer's basis is determined wholly by reference to the consideration paid for such assets.

Section 1.1060-1(c) (1) defines a seller's consideration as the amount in the aggregate, realized from selling the assets in the applicable asset acquisition under section 1001(b). Section 1060 provides no independent basis for determining the amount a taxpayer realizes on the sale of assets or the time such amount may be taken into account; the amount realized and the time such amount is taken into account are determined solely under generally applicable tax accounting principles. See sections 1001 and 461(h). Section 1.1060-1(c)(1) defines a purchaser's consideration as the amount, in the aggregate, of its cost of purchasing the assets in the applicable asset acquisition that is properly taken into account in basis. Section 1060 provides no independent basis for determining a taxpayer's cost of acquired assets; cost is determined solely under generally applicable rules of tax accounting.

The residual method is based on a division of assets into seven classes: Class I (generally consisting of cash and general deposit accounts held in banks, savings and loan associations, and other depository institutions), Class II (generally consisting of actively traded personal property such as U.S. government securities and publicly traded stock, but also including certificates of deposit and foreign currency even if they are not actively traded personal property), Class III (accounts receivable, mortgages, and credit card receivables from customers which arise in the ordinary course of business), Class IV (stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of taxpayer if on hand at the close of the

taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business), Class V (all assets other than Class I, II, III, IV, VI, and VII assets). For a special election to classify the assets in nonqualifying decommissioning funds under Class V rather than under Classes I and II, see section 1.338-6T (applicable for applicable asset acquisitions on or after September 15, 2004). Class VI (all § 197 intangibles, as defined in section 197, except goodwill and going concern value), and Class VII (goodwill and going concern value, whether or not they qualify as section 197 intangibles).

Consideration is first reduced by the amount of Class I assets transferred by the seller. The remaining consideration is then allocated among the Class II assets (pro rata, to the extent of their fair market value), then among the Class III assets (pro rata, to the extent of their fair market value), then among the Class IV assets (pro rata, to the extent of their fair market value), then among the Class V assets (pro rata, to the extent of their fair market value), then among the Class VI assets (pro rata, to the extent of their fair market value), and, finally, any remaining consideration is allocated among the Class VII assets (pro rata, according to their fair market value). Sections 1060-1(c)(2), 1.338-6(b)(1), and 1.338-6(b)(2).

If under general tax principles there is a subsequent adjustment to the consideration, e.g., if it is later determined that the actual amount of the liability assumed differs from the value that the parties assigned to such liability on the date of the applicable asset acquisition, that amount is allocated in a manner that produces the same allocation that would have been made at the time of the acquisition had such amount been paid or incurred on the acquisition date. Sections 1060-1(a), 1.1060-1(c)(2), and 1.338-7.

The Plant, together with its related equipment, operating assets and nonqualified nuclear decommissioning fund assets, constitute a trade or business in its Seller's hands and the gain or loss recognized by Seller with respect to those assets will be determined wholly by reference to the Seller's amount realized. Thus, the Seller's transfer of its c percent undivided ownership interest in the Plant, its equipment, operating assets and nonqualified fund assets to Buyer in exchange for cash, and the assumption of the decommissioning liability (except to the extent funded by the qualified funds) is an applicable asset acquisition as defined in section 1060 and the regulations thereunder. As such, the Federal tax treatment of the Facility's acquisition is determined under section 1060 and the regulations thereunder.

Accordingly, we conclude that Seller's gain or loss on the Sale of a proportionate amount of the purchased assets (excluding Seller's qualified nuclear decommissioning funds) to Buyer will equal the difference between a proportionate amount of Seller's tax basis of each asset and the amount realized with respect to that asset, taking into account the allocation of consideration pursuant to Code section 1060 and the Regulations promulgated there under. We conclude further that Seller's amount realized from the sale of the purchased assets (excluding Seller's qualified nuclear

decommissioning funds) will include the cash received from Buyer and a proportionate amount of the liabilities and obligations assumed by Buyer, including a proportionate amount of the liability to decommission the Plant (reduced by the amount of the decommissioning liability to be funded by the qualified nuclear decommissioning funds), to the extent such liabilities and obligations are taken into account as liabilities for federal income tax purposes.

Requested Ruling #6: *Pursuant to section 1.461-4(d)(5), for the taxable year that includes the date of the closing, Seller shall be entitled to a current deduction in an amount equal to the total of any amounts treated as realized by the Seller as a result of Buyer's assumption of a proportionate amount of Seller's liability for decommissioning the Plant.*

Section 461(a) states that, generally, any deduction or credit allowed by subtitle A of the Code shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income.

Section 1.446-1(c)(1)(ii)(A) provides that under an accrual method of accounting, a liability is incurred and generally taken into account for federal income tax purposes in the year in which all events have occurred that establish the fact of the liability, the amount of the liability can be determined with reasonable accuracy, and economic performance has occurred with respect to the liability.

Section 461(h) makes clear that generally the all events test is not treated as having been met any earlier than the taxable year in which economic performance has occurred with respect to a liability. *See also* section 1.461-4(a)(1).

Section 461(h)(2)(B) provides that in the case of a liability that requires the taxpayer to provide services, economic performance occurs as the taxpayer provides the services. Section 1.461-4(d)(4) provides that economic performance occurs with respect to such service liabilities as the taxpayer incurs costs in connection with the satisfaction of a liability.

Section 1.461-4(d)(5) provides an exception to the general economic performance rule for services where the taxpayer sells a trade or business. Where the purchaser expressly assumes a liability arising out of the taxpayer’s trade or business that the taxpayer but for the economic performance requirement would have been entitled to incur as of the date of the sale, economic performance with respect to the liability occurs as the amount of the liability is properly included in the amount realized on the sale by the taxpayer.

The first prong of the all events test requires that the fact of the liability be established at the time of the deduction. This prong of the all events test is satisfied in the instant case. Here, the Seller clearly has the obligation to decommission the Plant. The fact of this obligation arose many years ago, at the time the Seller obtained its

license to operate the Plant. *See* 10 C.F.R. § 50.33 and § 72.30, requiring the operator of a nuclear power plant to decommission it. Moreover, Congress recognized the existence of the decommissioning liability when, in 1984, it enacted sections 461(h) and 468A, noting that "[g]enerally, under Federal and State laws, utilities that operate nuclear power plants are obligated to decommission the plants at the end of their useful lives." H.R. Conf. Rep. No. 98-861, 877 (1984). *See also* S. Prt. No. 169, Vol. 1, 98th Cong., 2d Sess. 277 (1984).

The second prong of the all events test requires that the amount of the liability be reasonably determinable. Section 1.461-1(a)(2)(ii). This prong is also satisfied. In the instant case, the amount of the Seller's decommissioning liability has been determined by experts in the nuclear decommissioning liability. Their calculations have been reviewed and accepted by Commission A. In addition, there is support in the Code for finding that the amount of the decommissioning liability is reasonably determinable at the time of the sale. Section 468A generally permits a current deduction for a "ruling amount", based on the estimated future decommissioning expenses. To the extent the decommissioning costs are sufficiently determinable to entitle the utility to a deduction under section 468A, it is reasonably determinable to conclude that the costs also must be sufficiently determinable to satisfy the second prong of the all events test.

Given that the two prongs of the all events test are satisfied, economic performance with respect to the decommissioning liability occurs as of the date of the sale to the extent the liability is included in Seller's amount realized. Accordingly, for the taxable year that includes the date of the closing, the Seller will be entitled to a current deduction for the amount of its otherwise deductible decommissioning liability to the extent treated as included in the amount realized by Seller as a result of the Buyer's express assumption of the Seller's decommissioning liability.

Requested Ruling #7: *Buyer will have a tax basis in the assets purchased (excluding Buyer's qualified nuclear decommissioning funds) equal to the sum of the Purchase Price and a proportionate amount of the Assumed Liabilities that will be taken into account as liabilities for federal income tax purposes as of the closing date.*

Section 1012 provides in part that the basis of property shall be the cost of such property. In cases similar to the instant case, taxpayers have argued that the cost of acquiring the Seller's interests in a nuclear power plant and the related assets (including the decommissioning funds) includes the amount of the assumed decommissioning liability. In those cases, taxpayers have cited Crane v. Commissioner, 331 U.S. 1 (1947), and Commissioner v. Oxford Paper Co., 194 F.2d 190 (1952), as support for the proposition that for the purpose of determining basis, the cost of property generally includes assumed liabilities to which the acquired property is subject to the extent such liabilities can be accurately valued and are not contingent at the time of purchase. Since Buyer will pay cash and assume the liabilities and obligations of the Seller, which includes the decommissioning liabilities in connection with the acquisition of the Plant,

its total cost of the purchased assets (excluding the qualified nuclear decommissioning funds) will equal the cash paid plus the assumed liabilities and obligations.

However, the assumed decommissioning liability cannot be treated as incurred for any federal income tax purpose – including basis – until economic performance occurs with respect to that liability. Section 1.446-1(c)(1)(ii)(A). Thus, critical to determining whether Buyer is entitled to treat the future decommissioning liability as a component of its cost basis in the purchased assets at the time of the closing is deciding whether the liability will be incurred for tax purposes as of the closing. It will not. Economic performance does not occur with respect to a service liability such as the decommissioning obligation until and to the extent that costs are incurred in satisfaction of that liability. Section 1.461-4(d)(4). Because Buyer will not have performed any services relating to the decommissioning liability at the time of its purchase of the Plant, economic performance will not have occurred, and the liability will not have been incurred at that time for any purpose under the Code, including the cost basis provision of section 1012.

Accordingly, we conclude that, at the time of closing, Buyer will have a tax basis in the assets purchased (excluding the Buyer's qualified nuclear decommissioning funds) equal to the sum of the purchase price and the assumed liabilities that will be taken into account as liabilities for federal income tax purposes as of the closing date. The purchased assets and the liabilities incurred do not include the assets in the qualified nuclear decommissioning funds or the liability attributable to the qualified nuclear decommissioning funds, because the tax effect of the qualified nuclear decommissioning funds is determined under section 468A. Buyer will not be entitled to treat as a component of its cost basis at the time of the closing any amount attributable to the future decommissioning liability.

Requested Ruling #8: *Following the closing and for all periods after the closing when Buyer and Seller are parties to, and subject to the terms of, the Decommissioning Funds Collection Agreement, Seller will not realize income upon its receipt of the Decommissioning Collections.*

Section 61 defines gross income as all income from whatever source derived, including compensation for services such as fees, commissions, and similar items. However, the mere receipt and possession of money does not by itself constitute gross income. One such instance where the receipt of money does not result in gross income is the receipt of money by a person acting as an agent under the control of, and receiving the payment for the benefit of, another. For example, a rental agent does not have income upon receipt of a rental payment from a tenant because the agent is a mere conduit for the payment from the tenant to the owner. This concept has been applied in a variety of situations involving agents and other conduits. *See*, *for example*, Maryland Casualty Co. v. United States, 381 U.S. 342, 345 (1920) and Fogarty v. United States, 780 F.2d 1005 (Fed. Cir. 1986).

The position that the principal, and not the agent, is taxed on amounts received by the agent on the principal's behalf is embodied in numerous revenue rulings. For example, Rev. Rul. 74-581, 1974-2 C.B. 25, involved fees received by a law school's faculty members for their court-appointed representation of indigent defendants while participating in the university's clinical program. Each faculty member must agree, as a condition of participation in the program, that since the time spent in supervising work of students on these cases and in the representation of the client is part of the faculty member's teaching duties for which the faculty member is compensated by a total annual salary, all amounts received for such representation are to be endorsed over to the law school. The attorney-faculty members involved are working solely as agents of the law school, while supervising the law students within the scope of the clinical programs, and realize no personal gain from payments for their services in representing the indigent defendants. The revenue ruling thus holds that the payments received by the faculty members for their representation of clients while participating in the clinical program are not required to be included in their gross income. *See also* Rev. Rul. 69-274, 1974-1 C.B. 36; Rev. Rul. 65-282, 1965-1 C.B. 21; and Rev. Rul. 58-220, 1958-1 C.B. 26.

In the present case, under the Decommissioning Funds Collection Agreement mandated by Commission A, the Seller is required to continue to charge rates from Seller's regulated ratepayers for the purpose of collecting decommissioning monies to be remitted to Buyer's nuclear decommissioning trust funds. The purpose of the Decommissioning Funds Collection Agreement is to ensure that Buyer will have adequate funds to decommission the Generation Facility. The Decommissioning Funds Collection Agreement specifically provides that in collecting and remitting the decommissioning revenue, Seller shall act as Buyer's Collection Agent. Moreover, Seller receives no benefit from the Decommissioning Collections. Rather, Buyer is the intended recipient of, and the only party benefiting from, the collections. In the present case, under the Decommissioning Funds Collection Agreement, Seller is authorized to retain a portion of the Decommissioning Collections it receives, to the extent that the Decommissioning Collections include a recovery of administrative or other costs incurred by Seller.

Accordingly, based on the facts represented by Buyer and Seller, we conclude that, except as provided below, Seller will not realize income upon Seller's receipt of Decommissioning Collections after the closing of the sale. If, in accordance with the Decommissioning Funds Collection Agreement or for some other reason, Seller retains a portion of the Decommissioning Collections and does not remit all of such collections to Buyer, Seller must include the amount retained in its gross income.

Requested Ruling #9: *Following the closing and for all periods after the closing when Buyer and Seller are parties to, and subject to the terms of, the Decommissioning Funds Collection Agreement, Buyer will recognize income upon Seller's receipt of the Decommissioning Collections in accordance with section 88 and the regulations thereunder.*

In Requested Ruling #8 we determined that Seller acts as Buyer's agent when collecting amounts for the decommissioning of Plant from its retail customers that are required to be remitted to Buyer. Under the principles of agency, Buyer is deemed to be in receipt of these amounts at the time they are collected by Seller.

Section 88 provides that, in the case of any taxpayer who is required to include the amount of any nuclear decommissioning costs in the taxpayer's cost of service for ratemaking purposes, there shall be includible in the gross income of such taxpayer the amount so included for any taxable year.

The taxpayers have represented that Buyer will be a named recipient of, and will be bound by the terms of, all orders issued by Commission A establishing the cost of decommissioning Buyer's interest in the Plant and establishing the amount to be collected from ratepayers with respect to that cost. Consequently, and based upon the continued validity of that representation, we conclude that following the closing and for all periods after the closing when Buyer and Seller are parties to, and subject to the terms of, the Decommissioning Funds Collection Agreement, the income that Buyer recognizes upon Seller's receipt of the Decommissioning Collections shall be deemed to be income described in section 88 and the regulations thereunder.

Requested Ruling #10: *Following the closing and for all periods after the closing when Buyer and Seller are parties to, and subject to the terms of, the Decommissioning Funds Collection Agreement, Buyer will satisfy the "cost of service" requirement with respect to its qualified nuclear decommissioning funds within the meaning of section 468A and the regulations thereunder and, therefore, Buyer will be permitted to make deductible contributions to its qualified nuclear decommissioning funds for the Decommissioning Collections collected by the Seller through a nonbypassable charge and remitted directly or indirectly to Buyer's nuclear decommissioning funds in accordance with the rules of Commission A and the Decommissioning Funds Collection Agreement.*

The taxpayers have represented that Buyer will be a named recipient of, and will be bound by the terms of, all orders issued by Commission A establishing the cost of decommissioning Buyer's interest in the Plant and establishing the amount to be collected from ratepayers with respect to that cost. Consequently, and based upon the continued validity of that representation, we conclude that following the closing and for all periods after the closing when Buyer and Seller are parties to, and subject to the terms of, the Decommissioning Funds Collection Agreement, Buyer will be deemed to have satisfied the "cost of service" requirement with respect to its qualified nuclear decommissioning funds within the meaning of section 468A and the regulations thereunder and, therefore, Buyer will be permitted to make deductible contributions to its qualified nuclear decommissioning funds for the Decommissioning Collections collected by the Seller through a nonbypassable charge and remitted directly or

indirectly to Buyer's nuclear decommissioning funds in accordance with the rules of Commission A and the Decommissioning Funds Collection Agreement.

Requested Ruling #11: *In the taxable year of the closing, Buyer will not recognize any gain or loss or otherwise take any income into account by reason of the transfer of all or a portion of the assets of Seller's Nonqualified Decommissioning Funds to Buyer's nonqualified nuclear decommissioning funds.*

A taxpayer generally does not realize gross income upon its purchase of a business's assets, even where those assets include cash or marketable securities and, in connection with the purchase, the taxpayer assumes liabilities of the seller. Commissioner v. Oxford Paper, 194 F.2d 190 (2nd Cir. 1952); Rev. Rul. 55-675, 1955-2 C.B. 567. In this case, Buyer cannot acquire the Plant without assuming the decommissioning liability, which is inextricably associated with ownership and operation of the plant, and there is no indication that the transaction is other than a *bona fide* purchase of the business and its associated assets and liabilities. While an exception to the general rule that a taxpayer does not realize gross income upon its purchase of the assets of a business is set forth in Rev. Rul. 71-450, 1971-2 C.B. 78, such ruling does not apply to the present case. In Rev. Rul. 71-450, unlike the present situation, the purchaser agreed to assume a prepaid subscription liability in return for a separate cash payment, and the liability was not reflected in the sales price of the business. We assume that Buyer's basis attributable to the decommissioning liability is governed by section 461(h) and that the consideration furnished by Buyer will be allocated pursuant to the residual method under section 1060 and the regulations thereunder.

Accordingly, we conclude that in the taxable year of the closing, Buyer will not recognize any gain or loss or otherwise take any income into account by reason of the transfer of all or a portion of the assets of Seller's nonqualified nuclear decommissioning funds to Buyer's nonqualified nuclear decommissioning funds, except to the extent that, under the rules of section 1060, the amount of cash and other Class 1 assets received by Buyer exceeds the amount of consideration provided by Buyer and taken into account in the year of the acquisition.

Requested Ruling #12: *Buyer's nonqualified nuclear decommissioning funds are grantor trusts under section 671 and Buyer will be treated as the grantor of each trust.*

Section 671 provides that where it is specified in sections 673 through 678 that the grantor or another person shall be treated as the owner of any portion of a trust, there shall be included in computing the taxable income and credits of that person those items of income, deduction, and credits against tax of the trust which are attributable to that portion of the trust to the extent that such items would be taken into account in computing taxable income or credits against the tax of an individual.

Section 1.671-2(e)(1) provides that for purposes of part I of subchapter J, chapter 1 of the Internal Revenue Code, a grantor includes any person to the extent such

person either creates a trust, or directly or indirectly makes a gratuitous transfer (within the meaning of section 1.671-2(e)(2)) of property to a trust. For purposes of section 1.671-2, the term property includes cash.

Section 1.671-2(e)(2)(i) provides that a gratuitous transfer is any transfer other than a transfer for fair market value.

Section 1.671-2(e)(2)(ii) provides that for purposes of section 1.671-2(e), a transfer is for fair market value only to the extent of the value of property received from the trust, services rendered by the trust, or the right to use property of the trust.

Section 677 provides that the grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such under section 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a nonadverse party, or both, may be distributed to the grantor, or held or accumulated for future distribution to the grantor.

Section 1.677(a)-1(d) provides that under section 677 a grantor is, in general, treated as the owner of a portion of a trust whose income is, or in the discretion of the grantor or a nonadverse party, or both, may be applied in discharge of a legal obligation of the grantor.

Because Buyer is treated as purchasing the assets of Seller's nonqualified nuclear decommissioning funds for federal income tax purposes, Buyer is treated as contributing those assets as grantor to Buyer's respective nonqualified nuclear decommissioning funds. Under the terms of the trust agreement, all income, as well as principal of the Buyer's nonqualified nuclear decommissioning funds is held to satisfy Buyer's legal obligation to decommission each unit of the Plant. Accordingly, Buyer's nonqualified nuclear decommissioning funds are grantor trusts and Buyer is treated as the grantor and the owner of Buyer's nonqualified nuclear decommissioning funds under section 677 and section 1.677(a)-1(d). Buyer shall include in computing its taxable income and credits all items of income, deduction, and credits against tax of the Buyer's nonqualified nuclear decommissioning funds to the extent that such items would be taken into account in computing taxable income or credits against the tax of Buyer.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer. A copy of this letter must be attached to any income tax return to which it is relevant.

Sincerely,

Peter C. Friedman
Senior Technician Reviewer, Branch 6
(Passthroughs & Special Industries)

cc: