Internal Revenue Service

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Department of the Treasury
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Person To Contact:
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Date:
November 2, 2006

Legend:

Taxpayer =

Plant =
State =
Parent =
Location =
Subsidiary =
Former Owner One =
Former Owner Two =
Method =
Commission =
Order One =
Order Two =
Order Three =
Date One =
Date Two =
Date Three =
a =
b =
c =
d =
e =
f =
g =
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Dear :

This letter responds to your letter dated November 23, 2005, and subsequent submissions, requesting a revised schedule of ruling amounts pursuant to § 1.468A-3(i) of the Income Tax Regulations. A schedule of ruling amounts was previously issued with regard to Taxpayer's interests in the Plant on Date One and Date Two. Information was submitted pursuant to § 1.468A-3(h)(2).

Taxpayer represents the facts and information relating to its request for a revised schedule of ruling amounts as follows:

Taxpayer is a corporation organized and incorporated under the laws of State, and is principally engaged in the generation and sale of electric energy in State. All of the outstanding common stock of Taxpayer is held by Parent. Taxpayer files its Federal income tax return on a calendar year basis using the accrual method of accounting.

Plant is situated at Location. In a, Taxpayer acquired b percent of the Plant in the context of Taxpayer's purchase of the outstanding stock of Former Owner One (the "Historic Interest"). In c, Taxpayer purchased an additional d percent interest in Plant, including a proportionate amount of the associated nuclear decommissioning funds, from Former Owner Two (the "Acquired Interest"). Accordingly, Taxpayer currently owns a total e percent undivided interest in Plant, which is held by Subsidiary, an indirect subsidiary of Taxpayer. Subsidiary is directly owned by two limited liability companies that are, in turn, wholly owned by Taxpayer. The two limited liability companies and Subsidiary are all treated as disregarded entities for Federal income tax purposes. Consequently, Subsidiary is treated as a division of Taxpayer, and Taxpayer is treated as the direct owner Subsidiary's interest in Plant.

The estimated base cost for decommissioning Plant is based on an independent study and the proposed method of decommissioning the Plant is Method.

As a current owner of the Historic Interest and the Acquired Interest, Subsidiary is a party to two trust agreements for purposes of establishing and maintaining funds for the purpose of decommissioning Plant. The laws of State require that the funds relating to the Historic Interest and the Acquired Interest be maintained separately, and on Date Three, the Internal Revenue Service issued private letter rulings in which the Service concluded that Taxpayer may maintain such separate funds without disqualification, and that the funds would be treated as a single fund for purposes of section 468A.

State law states that, following a transfer of State jurisdictional nuclear generating plant assets, including the associated nuclear decommissioning trust funds, any remaining costs associated with nuclear decommissioning obligations shall remain subject to cost-of-service regulation based on periodic review of such costs.

Historic Interest

Pursuant to the requirements of State law, Taxpayer and Former Owner One entered into a decommissioning funds collection agreement ("Agreement One"), under which Former Owner One continues to collect decommissioning costs associated with the Historic Interest from its ratepayers and remits such actual collections directly or indirectly to Taxpayer's funds on a weekly basis. The Internal Revenue Service determined in a private letter ruling that, under this arrangement, Taxpayer will be deemed to have satisfied the "cost-of-service" requirement with respect to its funds and, therefore, will be permitted to make deductible contributions to its qualified nuclear decommissioning funds for the amounts collected by Former Owner One through a nonbypassable charge and remitted to Taxpayer's funds under Agreement One.

The amount of the nonbypassable charge collected by Former Owner One is determined by means of a formula set forth in a tariff approved by Commission. The formula was developed in order that the collected amounts are consistent with the underlying principles of section 468A, such as the level-funding requirement.

The after-tax fair market value of the assets in the portion of the qualified nuclear decommissioning fund that relates to the historic interest as of the period to which the proposed schedule of ruling amounts relates was approximately f. The after-tax rate of return earned by the assets of this portion of the fund since its formation is g percent. The estimated base cost of decommissioning the Historic Interest is h. The Commission then escalated the base cost at i percent resulting in a total estimated future decommissioning cost of the Historic Interest of j. Decommissioning costs are expected to be collected through k, and the funding period and level funding limitation period both extend through k. The qualified percentage for the fund is l percent. The

dollar amount that is expected to be earned by the fund, during the period beginning on the first date to which the revised schedule of ruling amounts applies and ending on the last day of the funding period, is m.

In Order, the Commission authorized a total annual decommissioning cost collection amount, and the Taxpayer's share of this amount for the Historic Interest in Plant is n.

Acquired Interest

Pursuant to the requirements of State law, Taxpayer and Former Owner Two entered into a decommissioning funds collection agreement ("Agreement Two"), under which Former Owner Two continues to collect decommissioning costs associated with the Historic Interest from its ratepayers and remits such actual collections directly or indirectly to Taxpayer's funds on a weekly basis. The Internal Revenue Service determined in a private letter ruling that, under this arrangement, Taxpayer will be deemed to have satisfied the "cost-of-service" requirement with respect to its funds and, therefore, will be permitted to make deductible contributions to its qualified nuclear decommissioning funds for the amounts collected by Former Owner Two through a nonbypassable charge and remitted to Taxpayer's funds under Agreement Two.

The amount of the nonbypassable charge collected by Former Owner Two is determined by means of a formula set forth in a tariff approved by Commission. The formula was developed in order that the collected amounts are consistent with the underlying principles of section 468A, such as the level-funding requirement.

The after-tax fair market value of the assets in the portion of the qualified nuclear decommissioning fund that relates to the historic interest as of the period to which the proposed schedule of ruling amounts relates was approximately o. The after-tax rate of return earned by the assets of this portion of the fund since its formation is p percent. The estimated base cost of decommissioning the Acquired Interest is q. In Order Two, the Commission then escalated the base cost at r percent resulting in a total estimated future decommissioning cost of the Acquired Interest of s. In Order Three, the Commission escalated the base cost at t percent resulting in a total estimated future decommissioning cost of the Acquired Interest of u. Decommissioning costs are expected to be collected through v, and the funding period and level funding limitation period both extend through v. The qualified percentage for the fund is w percent. The dollar amount that is expected to be earned by the fund, during the period beginning on the first date to which the revised schedule of ruling amounts applies and ending on the last day of the funding period, is x.

In Order Two, the Commission authorized a total annual decommissioning cost collection amount, and the Taxpayer's share of this amount for the Acquired Interest in Plant is y. In Order Three, the Commission authorized a total annual decommissioning

cost collection amount, and the Taxpayer's share of this amount for the Acquired Interest in Plant is z.

Formula Basis for Ruling Amounts

Law and Analysis

Section 468A provides that a taxpayer may elect to deduct the amount of payments made to a qualified decommissioning fund. However, § 468A(b) limits the amount paid into such fund for any taxable year to the lesser of the amount of nuclear decommissioning costs allocable to this fund which is included in the taxpayer's cost of service for ratemaking purposes for the tax year or the ruling amount applicable to this year.

Section 468A(d)(1) provides that no deduction shall be allowed for any payment to the nuclear decommissioning fund unless the taxpayer requests and receives from the Secretary a schedule of ruling amounts. The "ruling amount" for any tax year is

defined under § 468A(d)(2) as the amount which the Secretary determines to be necessary to fund that portion of nuclear decommissioning costs which bears the same ratio to the total nuclear decommissioning costs with respect to the nuclear power plant as the period for which the nuclear decommissioning fund is in effect bears to the estimated useful life of the plant. This term is further defined to include the amount necessary to prevent excessive funding of nuclear decommissioning costs or funding of these costs at a rate more rapid than level funding, taking into account such discount rates as the Secretary deems appropriate.

Section 468A(g) provides that a taxpayer shall be deemed to have made a payment to the nuclear decommissioning fund on the last day of a taxable year if the payment is made on account of such taxable year and is made within 2 1/2 months after the close of the tax year.

Section 1.468A-1(a) provides that an eligible taxpayer may elect to deduct nuclear decommissioning costs under section 468A of the Code. An "eligible taxpayer," as defined under § 1.468A-1(b)(1) of the regulations, is a taxpayer that has a "qualifying interest" in, among other things, a direct ownership interest.

Section 1.468A-1(b)(2)(ii) provides that the term "qualifying interest" means a leasehold interest in any portion of a nuclear power plant if: (A) The holder of the leasehold interest is subject to the jurisdiction of a public utility commission with respect to such portion of the nuclear power plant; (B)The holder of the leasehold interest is primarily liable under Federal or State law for decommissioning such portion of the nuclear power plant; and (C) No other person establishes a nuclear decommissioning fund with respect to such portion of the nuclear power plant.

Section 1.468A-2(b)(1) provides that the maximum amount of cash payments made (or deemed made) to a nuclear decommissioning fund during any tax year shall not exceed the lesser of the cost of service amount applicable to the nuclear decommissioning fund for such tax year; or the ruling amount applicable to the nuclear decommissioning fund for such tax year.

Section 1.468A-3(a)(1) provides that, in general, a schedule of ruling amounts for a nuclear decommissioning fund is a ruling specifying annual payments that, over the tax years remaining in the "funding period" as of the date the schedule first applies, will result in a projected balance of the nuclear decommissioning fund as of the last day of the funding period equal to (and in no event more than) the "amount of decommissioning costs allocable to the fund".

Section 1.468A-3(a)(4) provides that the Internal Revenue Service shall approve, at the request of the taxpayer, a formula or method of determining a schedule of ruling amounts (rather than a schedule specifying a dollar amount for each taxable year) that is consistent with the principals and provisions of § 1.468A-3.

Section 1.468A-3(b)(1) provides that, in general, the amount for any tax year in the level funding limitation period shall not be less than the ruling amount for any earlier tax year. Under § 1.468A-3(b)(2), the level funding limitation period begins on the first day of the first tax year for which a deductible payment is made to the nuclear decommissioning fund and ends on the last day on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes.

Section 1.468A-3(d)(1) provides that the amount of decommissioning costs allocable to a nuclear decommissioning fund is the taxpayer's share of the total estimated cost of decommissioning the nuclear power plant multiplied by the qualifying percentage.

Section 1.468A-3(d)(2) provides that, in general, the total estimated cost of decommissioning a nuclear power plant is the reasonably estimated cost of decommissioning used by the applicable public utility commission in establishing or approving the amount of these costs to be included in cost of service for ratemaking purposes.

Section 1.468A-3(d)(3) provides that a taxpayer's share of the total estimated cost of decommissioning a nuclear power plant equals the total estimated cost of decommissioning such plant multiplied by the taxpayer's qualifying interest in the plant. Under § 1.468A-3(d)(4), the qualifying percentage for any nuclear decommissioning fund is equal to a fraction, the numerator of which is the number of tax years in the estimated period for which the nuclear decommissioning fund is to be in effect and the denominator of which is the number of tax years in the estimated useful life of the applicable plant.

Section 1.468A-3(d)(4)(ii) provides that the estimated period for which a nuclear decommissioning fund is to be in effect begins on the later of (1) the first day of the first taxable year for which a deductible payment is made to the nuclear decommissioning fund (or deemed made); or (2) the first day of the taxable year that includes the date that the nuclear power plant begins commercial operations (as determined by the applicable public utility commission at the time the plant was first included in the taxpayer's rate base); and ends on the last day of the taxable year that includes the estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes. According to § 1.468A-3(e)(3), the estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes is determined under the ratemaking assumptions used by the applicable public utility commission in establishing or approving rates during the first ratemaking proceeding in which the nuclear power plant was included in the taxpayer's rate base.

Section 1.468A-3(d)(4)(iii) provides that the estimated useful life of a nuclear power plant begins on the first day of the taxable year that includes the date that the plant begins commercial operations (as determined by the applicable public utility commission at the time the plant was first included in the taxpayer's rate base); and ends on the last day of the taxable year that includes the estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes. According to § 1.468A-3(e)(3), the estimated date on which the nuclear power plant will no longer be included in the taxpayer's rate base for ratemaking purposes is determined under the ratemaking assumptions used by the applicable public utility commission in establishing or approving rates during the first ratemaking proceeding in which the nuclear power plant was included in the taxpayer's rate base.

Section 1.468A-3(g) provides that the Internal Revenue Service shall not provide a taxpayer with a schedule of ruling amounts for any nuclear decommissioning fund unless the public utility commission that establishes or approves the rates for electric energy generated by the plant has determined the amount of decommissioning costs to be included in the taxpayer's cost of service for ratemaking purposes and has disclosed the after-tax rate of return and any other assumptions and determinations used in establishing or approving the amount.

Section 1.468A-3(h)(2) enumerates the information required to be contained in a request for a schedule of ruling amounts filed by a taxpayer in order to receive a ruling amount for any taxable year.

Section 1.468A-3(i)(1)(ii) provides that any taxpayer that has obtained a formula or method for determining a schedule of ruling amounts for any taxable year must file a request for a revised schedule on or before the earlier of the deemed payment deadline for the fifth taxable year that begins after the taxable year in which the most recent formula or method was approved, or the deemed payment deadline date for the first taxable year that begins after a taxable year in which there is a substantial variation in the ruling amount determined under the most recent formula or method. There is a substantial variation if the ruling amount for the year and the ruling amount for any earlier year since the most recent formula or method was approved differ by more than 50 percent of the smaller amount.

We have examined the representations and information submitted by the Taxpayer in relation to the requirements set forth in § 468A and the regulations thereunder. Based solely upon these representations of the facts, we reach the following conclusions:

1. Taxpayer has a qualifying interest in the Plant and is, therefore, an eligible taxpayer under § 1.468A-1(b)(1) of the regulations.

2. Commission has determined the amount of decommissioning costs to be included in cost of service for ratemaking purposes as required by § 1.468A-3(g) of the regulations.

3. Taxpayer, as owner of the Plant, has calculated its share of the total decommissioning costs under § 1.468A-3(d)(3) of the regulations.

4. Taxpayer has determined that, pursuant to § 1.468A-3(d)(4) of the regulations, the qualifying percentage is l percent for the Historic Interest, and w percent for the Acquired Interest.

5. Taxpayer has calculated its share of the total decommissioning costs, as required by § 1.468A-(3)(f)(2) of the regulations.

6. Pursuant to § 1.468A-3(a)(4)of the regulations, we approve a formula for determining the schedule of ruling amounts (rather than a schedule specifying a dollar amount for each taxable year) that is consistent with the principles and provisions of section 468A.

Based solely on the determinations above, we conclude that the Taxpayer's proposed schedule of ruling amounts satisfies the requirements of § 468A of the Code.

APPROVED SCHEDULE OF RULING AMOUNTS FOR TAXABLE YEARS

Approval of the schedule of ruling amounts is contingent on there being no change in the facts and circumstances, known or assumed, at the time the current ruling is issued. If any of the events described in § 1.468A-3(i)(1)(iii) occur in future years, the Taxpayer must request a review and revision of the schedule of ruling amounts. Generally, the Taxpayer is required to file such a request on or before the deemed payment deadline date for the first taxable year in which the rates reflecting such action became effective. When no such event occurs, the Taxpayer must file a request for a revised schedule on or before the earlier of the deemed payment deadline for the fifth taxable year that begins after the taxable year in which the most recent formula or method was approved, or the deemed payment deadline date for the first taxable year that begins after a taxable year in which there is a substantial variation in the ruling amount determined under the most recent formula or method. There is a substantial variation if the ruling amount for the year and the ruling amount for any earlier year

since the most recent formula or method was approved differ by more than 50 percent of the smaller amount.

Except as specifically determined above, no opinion is expressed or implied concerning the Federal income tax consequences of the transaction described above.

The approved schedule of ruling amounts is relevant only to those payments made to the Fund. Payments allocable to any funds other than the Fund, cannot qualify for purposes of the deduction under the provisions of § 468A of the Code. Payments made to such Fund can qualify only to the extent that they do not exceed the lesser of the decommissioning costs applicable to such Fund or the ruling amounts applicable to this Fund in the tax year.

This ruling is directed only to the Taxpayer who requested it. Effective January 1, 2006, amendments were made to § 468A by the Energy Tax Incentives Act of 2005, Pub. L. 109-58, 119 Stat. 594. Regulations based on these amendments are being developed but have not yet been proposed. Because the period to which the schedule of ruling amounts above relates began prior to the effective date of these amendments, the discussion above is based on the law in effect prior to January 1, 2006. However, this ruling will be modified or revoked by the adoption of temporary or final regulations to the extent the regulations are inconsistent with any conclusion in the letter ruling. See section 11.04 of Rev. Proc. 2006-1, 2006-1 I.R.B. 1, 49. However, when the criteria in section 11.05 of Rev. Proc. 2006-1, 2006-1 I.R.B. 49 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

Section 6110(k)(3) of the Code provides 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. We are also sending a copy of this letter ruling to the Industry Director, Natural Resources and Construction (LM:NRC). Pursuant to § 1.468A-7(a), a copy of this letter must be attached (with the required Election Statement) to the Taxpayer's federal income tax return for each tax year in which the Taxpayer claims a deduction for payments made to the Fund.

Sincerely,

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