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Date:
December 21, 2011

Re: Request for Private Letter Ruling under Section 168(k)

Taxpayer =
Contract =

State1 =
City1 =
A =
B =
C =
D =
E =
F =
G =
H =
I =
J =
K =
Number1 =
Number2 =
Number3 =
Number4 =
Number5 =
Number6 =
Number7 =
Year1 =
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Year3 =
Date1 =
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Date5 =
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Date8 =
Date9 =

Dear :

This letter responds to a letter dated June 27, 2011, submitted by Taxpayer requesting rulings under section 168(k) of the Internal Revenue Code.

FACTS

Taxpayer represents that the facts are as follows:

Taxpayer is a limited liability company that is Number1-percent owned by A, a limited liability company that is a disregarded entity for Federal income tax purposes (a "disregarded entity"). A is Number1-percent owned by B. Through the Year1 taxable year, Taxpayer was treated as a disregarded entity. Taxpayer elected to be treated as a separate corporation effective for the Year2 calendar year. For its initial federal income tax return, Taxpayer is adopting a method of accounting for purposes of section 1.461-4(d)(6)(iii) of the Income Tax Regulations that will treat property as provided to Taxpayer when the property is accepted by Taxpayer.

B is a corporation organized and incorporated under the laws of State1 that, directly or indirectly, owns several regulated and unregulated energy companies. Taxpayer and D, among other entities, join in the consolidated federal income tax return filed for the affiliated group headed by B. B files its consolidated return on a calendar year end basis. Taxpayer's and B's overall method of accounting is the accrual method.

D is a public utility providing electric, gas, and steam service to customers and is subject to the regulatory jurisdiction of the E, the F, and the G. D is a wholly-owned subsidiary of B.

Taxpayer was formed to own two Number2 megawatts units to be located adjacent to the site of the existing C owned by D. In Date1, the E issued an order granting Taxpayer, B, and D the right to construct these two units. I, as agent for Taxpayer, and H entered into a Contract dated Date2. I is a disregarded entity that is Number1-percent owned by A.

Taxpayer represents that the Contract is a written binding contract under the law of State1, which is the governing law under the Contract. Further, Taxpayer represents that the Contract did not limit damages to an amount that is less than five percent of the Contract price.

Under the Contract, H was to construct on a lump sum, fixed priced turnkey basis two nominal Number2 megawatts electric generating units (hereinafter, the two units separately are referred to as "Unit 1" and "Unit 2," and the two units together are referred to as the "Units") and certain related equipment and facilities (the "Common Facilities"). Hereinafter, the Units and the Common Facilities together are referred to as the "Facility". The Facility is located in City1, State1.

Taxpayer has full responsibility and liability for payment under the Contract. Under the Contract, Taxpayer may terminate the Contract for its convenience at any time by notice to H indicating the termination date. Upon cancellation, Taxpayer must compensate H for all payment events completed up to the date of termination and that had not previously been paid to H and an amount mutually agreed to for the completed percentage of partially completed payment events, costs incurred by H to demobilize the Facility site and costs incurred by H in terminating contracts with subcontractors.

The Contract price was the lump sum turnkey price of initially $Number3. Payment under the Contract was made by Taxpayer according to a payment schedule based on payment events.

The Contract was subject to a number of change orders. On Date3, H submitted claims for schedule and cost relief related to the delay of the in-service dates for Unit 1 and Unit 2. This claim was amended on Date4. Effective Date5, Taxpayer and H entered into a Settlement Agreement and Release (the "Settlement Agreement") that settled all claims regarding Unit 1 and Unit 2. Under the Settlement Agreement, the Contract price for the Facility was increased by $Number4 and the Guaranteed Turnover Dates under the Contract were extended for Number5 days for Unit 1 and Number6 days for Unit 2. None of the amendments to the Contract changed the location of the Facility or the nominal nameplate capacity of either Unit 1 or Unit 2.

H commenced construction under the Contract in Date6. By this time, Taxpayer had made payments to H of approximately $Number7 under the Contract. If Taxpayer had terminated the Contract, then it would be required to pay H additional amounts that would have equaled, when added together with the $Number8 paid, more than five percent of the Contract price.

Section 1.2 of the Contract defines the term "turnover" as meaning "a) the completion of all Work by [H] and other requirements of Article 12 (Completion Sequence) that are conditions to the turning-over of a Phase and b) the transfer of care, custody and control and risk of loss of a Phase to [Taxpayer] or, at [Taxpayer's] direction, to [D] pursuant to the terms and conditions of this Contract". Section 15.1 of the Contract provides that title to work passes from H upon the work being identified as ready for shipment at the manufacture/fabrication site. Section 15.2 of the Contract provides that: (i) risk of loss for each phase of the Facility shall pass from H at turnover of such phase; (ii) prior to the turnover of any phase, H is obligated to replace, repair, or reconstruct any part of the Facility that is lost, damaged, or destroyed; and (iii) from and after the turnover, Taxpayer assumes all risk of loss or damage to the phase turned-over.

There were three phases under the Contract--the Common Facilities, Unit 1, and Unit 2. Turnover of each phase occurred upon the completion of all work by H and the transfer of care, custody and control and risk of loss of that phase to Taxpayer. Turnover of each of the Units occurred separately, as did turnover of certain Common Facilities. Turnover of a Common Facility, a that serves the existing units, occurred in Year3, and was placed in service during Year3. Turnover of a second Common Facility, a that serves the existing units, occurred in Year1, and this was placed in service during Year1. Taxpayer represents that these two Common Facilities do not qualify for any additional first year depreciation under section 168(k).

Turnover of Unit 1 occurred on Date7, when commercial operation was reached. Taxpayer represents that Unit 1 was originally placed in service on Date7, and that Taxpayer was the original user of Unit 1. Turnover of Unit 2 occurred on Date8, when commercial operation of this unit was reached. Taxpayer represents that Unit 2 was originally placed in service on Date8, and that Taxpayer was the original user of Unit 2.

Taxpayer leased its undivided interest in the Facility to D in a lease that is treated as a true lease for Federal income tax purposes. The lease with respect to each Unit commenced on the date it was first placed in service.

In addition to the costs incurred by H, Taxpayer and its affiliates incurred a small amount of other costs for items like permitting, project development, project design, engineering, preconstruction, construction management, and troubleshooting costs. Taxpayer represents that with respect to Unit 1, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of January 1, 2008, were 10 percent or less of the final tax basis of Unit 1 as of the original placed-in-service date. Taxpayer represents that the prior sentence is not altered even if one accrues capitalized interest on costs incurred by Taxpayer and payments made to H through January 1, 2008.

Taxpayer represents that with respect to Unit 2, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of January 1, 2008, were 10 percent or less of the final tax basis of Unit 2 as of the original placed-in-service date. Taxpayer represents that the prior sentence is not altered even if one accrues capitalized interest on costs incurred by Taxpayer and payments made to H through January 1, 2008.

Taxpayer represents that with respect to Unit 2, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of September 9, 2010, excluding any capitalized interest, were 10 percent or less of the final tax basis of Unit 2 as of the original placed-in-service date.

Pursuant to a telephone conversation on Date9, between Taxpayer's representative, J, and K of this office, J said that he believes that with respect to Unit 2, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of September 9, 2010, including any capitalized interest, were probably more than 10 percent of the final tax basis of Unit 2 as of the original placed-in-service date.

Taxpayer represents that both Unit 1 and Unit 2 are described in asset class 49.13 of Rev. Proc. 87-56, 1987-2 C.B. 674. Also, Taxpayer represents that Unit 1 and Unit 2 may include a small amount of transmission property that is described in asset class 49.14 of Rev. Proc. 87-56. Moreover, Taxpayer represents that the property subject to this ruling request with respect to Unit 1 and Unit 2 are not required to be depreciated under the alternative depreciation system of section 168(g).

RULINGS REQUESTED

1. Unit 1 and Unit 2 are each self-constructed property as defined in section 1.168(k)-1(b)(4)(iii)(A).

2. The fact that Taxpayer and H entered into the Contract prior to January 1, 2008, does not prevent Unit 1 and Unit 2 from meeting the acquisition requirements in sections 168(k)(2)(A)(iii) and (E)(i).

3. For purposes of determining for each of the Units when physical work of a significant nature begins under the safe harbor under section 1.168(k)-1(b)(4)(iii)(B)(*2*), no costs are incurred by Taxpayer under the Contract until turnover (as defined in the Contract) has occurred. As a result, no costs attributable to the Contract were incurred before (a) Date7, in the case of Unit 1, when turnover of Unit 1 occurred, and (b) Date8, in the case of Unit 2, when turnover of Unit 2 occurred.

4. For purposes of section 1.168(k)-1(b)(4)(iii)(B)(*2*), construction of Unit 1 began after December 31, 2007.

5. For purposes of section 1.168(k)-1(b)(4)(iii)(B)(*2*), construction of Unit 2 began after December 31, 2007.

6. The section 1245 property at Unit 1 qualifies for the 50-percent additional first year depreciation allowance under section 168(k)(1).

7. The section 1245 property at Unit 2 qualifies for the 50-percent additional first year depreciation allowance under section 168(k)(1). If a proper election is made pursuant to section 3.02(2)(b) of Rev. Proc. 2011-26, 2011-16 I.R.B. 664, any components of Unit 2 acquired or self-constructed by Taxpayer after September 8, 2010, qualify for the 100-percent additional first year depreciation allowance under section 168(k)(5).

LAW AND ANALYSIS

Section 168(k)(1)(A) (as amended by the Economic Stimulus Act of 2008, Pub. L. No. 110-185, 122 Stat. 613 (February 13, 2008) ("Stimulus Act")) provides a 50-percent additional first year depreciation deduction for the taxable year in which qualified property is placed in service by a taxpayer.

Section 168(k)(2)(A) (as amended by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296 (December 17, 2010) ("TRUIRJCA")) defines the term "qualified property" as meaning property (i) among other things, to which section 168 applies with a recovery period of 20 years or less, (ii) the original use of which commences with the taxpayer after December 31, 2007, (iii) that is acquired by the taxpayer after December 31, 2007, and before January 1, 2013, but only if no written binding contract for the acquisition was in effect before January 1, 2008, or that is acquired by the taxpayer pursuant to a written binding contract which was entered into after December 31, 2007, and before January 1, 2013, and (iv) that is placed in service by the taxpayer before January 1, 2013, or in the case of property described in section 168(k)(2)(B) or (C), before January 1, 2014.

For purposes of section 168(k)(2)(A)(i), section 1.168(k)-1(b)(2)(i)(A) provides that the recovery period is determined in accordance with section 168(c) regardless of any election made by the taxpayer under section 168(g)(7). The recovery period under section 168(c) is determined by the property's classification under section 168(e).

For purposes of section 168(e), a property's classification is determined by reference to the property's class life or by statute. Section 168(e)(1) provides that property with a class life of 25 or more years is 20-year property.

Section 168(i)(1) defines the term "class life" as meaning the class life (if any) that would be applicable with respect to any property as of January 1, 1986, under section 167(m) (determined without regard to section 167(m)(4) and as if the taxpayer had made an election under section 167(m)) as in effect on the day before the date of enactment of the Revenue Reconciliation Act of 1990. Former section 167(m) provided that in the case of a taxpayer who elected the Class Life Asset Depreciation Range ("ADR") system of depreciation, the depreciation allowance was based on the class life prescribed by the Secretary that reasonably reflected the anticipated useful life of that class of property to the industry or other group.

Section 1.167(a)-11(b)(4)(iii)(*b*) provides rules for classifying property under former section 167(m). Property is included in the asset guideline class for the activity in which the property is primarily used. Property is classified according to primary use even though the activity in which the property is primarily used is insubstantial in relation to all the taxpayer's activities.

Section 1.167(a)-11(e)(3)(iii) provides that in the case of a lessor of property, unless there is an asset guideline class in effect for lessors of such property, the asset guideline class for such property is determined as if the property were owned by the lessee. However, in the case of an asset guideline class based upon the type of property (such as trucks or railroad cars) as distinguished from the activity in which used, the property is classified without regard to the activity of the lessee.

Rev. Proc. 87-56 sets forth the class lives of property that are necessary to compute the depreciation allowance under section 168. This revenue procedure establishes two broad categories of depreciable assets: (1) asset classes 00.11 through 00.4 that consist of specific depreciable assets used in all business activities; and (2) asset classes 01.1 through 80.0 that consist of depreciable assets used in specific business activities. An asset that falls within both an asset group (that is, asset classes 00.11 through 00.4) and an activity group (that is, asset classes 01.1 through 80.0) would be classified in the asset group. See Norwest Corp. & Subs. v. Commissioner, 111 T.C. 105, 156-64 (1998). The asset classes described below are set forth in Rev. Proc. 87-56.

Asset class 49.13, Electric Utility Steam Production Plant, of Rev. Proc. 87-56, includes assets used in the steam power production of electricity for sale, combustion turbines operated in a combined cycle with a conventional steam unit and related land improvements. Asset class 49.13 also includes package boilers, electric generators and related assets such as electricity and steam distribution systems as used by a waste reduction and resource recovery plant if the steam or electricity is normally for sale to others. Assets in class 49.13 have a class life of 28 years and, in accordance with section 168(e)(1), are classified as 20-year property. Pursuant to section 168(c), the recovery period for 20-year property is 20 years.

Asset class 49.14, Electric Utility Transmission and Distribution Plant, of Rev. Proc. 87-56, includes assets used in the transmission and distribution of electricity for sale and related land improvements. Asset class 49.14 excludes initial clearing and grading land improvements are specified in Rev. Rul. 72-403, 1972-2 C.B. 102. Assets in class 49.14 have a class life of 30 years and, in accordance with section 168(e)(1), are classified as 20-year property. Pursuant to section 168(c), the recovery period for 20-year property is 20 years.

Section 168(k)(2)(E)(i) (as amended by the TRUIRJCA) provides that in the case of a taxpayer manufacturing, constructing, or producing property for the taxpayer's own use, the requirements of section 168(k)(2)(A)(iii) shall be treated as met if the taxpayer begins manufacturing, constructing, or producing the property after December 31, 2007, and before January 1, 2013.

With the exception of the increased amount and the revised dates, the rules for determining whether depreciable property is eligible for the 50-percent additional first year depreciation deduction are the same as the rules in section 168(k) in effect before the enactment of the Stimulus Act. Accordingly, rules similar to the rules in section 1.168(k)-1 for "qualified property" or for "30-percent additional first year depreciation deduction" apply. *See* section 5.01 of Rev. Proc. 2008-54, 2008-2 C.B. 722.

Section 1.168(k)-1(b)(4)(i) provides the rules relating to section 168(k)(2)(A)(iii) [the acquisition requirement] and section 1.168(k)-1(b)(4)(iii) provides the rules relating to section 168(k)(2)(E)(i) [self-constructed property].

For purposes of the 50-percent additional first year depreciation deduction, section 1.168(k)-1(b)(4)(i) provides that depreciable property will meet the requirements of section 1.168(k)-1(b)(4) if the property is: (*1*) acquired by the taxpayer after [December 31, 2007], and before [January 1, 2013], but only if no written binding contract for the acquisition of the property was in effect before [January 1, 2008]; or (*2*) acquired by the taxpayer pursuant to a written binding contract that was entered into after [December 31, 2007], and before [January 1, 2013]. Section 1.168(k)-1(b)(4)(ii) defines a binding contract.

Section 1.168(k)-1(b)(4)(ii) defines a binding contract. Pursuant to section 1.168(k)-1(b)(4)(ii)(A), a contract is binding only if it is enforceable under State law against the taxpayer or a predecessor, and does not limit damages to a specified amount (for example, by use of a liquidated damages provision). For this purpose, a contractual provision that limits damages to an amount equal to at least 5 percent of the total contract price will not be treated as limiting damages to a specified amount. In determining whether a contract limits damages, the fact that there may be little or no damages because the contract price does not significantly differ from fair market value will not be taken into account. For example, if a taxpayer entered into an irrevocable written contract to purchase an asset for $100 and the contract contained no provision for liquidated damages, the contract is considered binding notwithstanding the fact that the asset has a fair market value of $99 and under local law the seller would only recover the difference in the event the purchaser failed to perform. If the contract provided for a full refund of the purchase price in lieu of any damages allowable by law in the event of breach or cancellation, the contract is not considered binding.

Section 1.168(k)-1(b)(4)(ii)(B) provides, in part, that a contract will continue to be binding if the parties make insubstantial changes in its terms and conditions or because any term is to be determined by a standard beyond the control of either party.

Section 1.168(k)-1(b)(4)(iii)(A) provides that if a taxpayer manufactures, constructs, or produces property for use by the taxpayer in its trade or business (or for its production of income), the acquisition rules in section 1.168(k)-1(b)(4)(i) are treated as met for qualified property if the taxpayer begins manufacturing, constructing, or producing the property after [December 31, 2007], and before [January 1, 2013]. This regulation further provides that property that is manufactured, constructed, or produced for the taxpayer by another person under a written binding contract (as defined in section 1.168(k)-1(b)(4)(ii)) that is entered into prior to the manufacture, construction, or production of the property for use by the taxpayer in its trade or business (or for its production of income) is considered to be manufactured, constructed, or produced by the taxpayer.

Section 1.168(k)-1(b)(4)(iii)(B)(*1*) provides that for purposes of section 1.168(k)-1(b)(4)(iii), manufacture, construction, or production of property begins when physical work of a significant nature begins. Physical work does not include preliminary activities such as planning or designing, securing financing, exploring, or researching. The determination of when physical work of a significant nature begins depends on the facts and circumstances.

Section 1.168(k)-1(b)(4)(iii)(B)(*2*) provides that for purposes of section 1.168(k)-1(b)(4)(iii)(B)(*1*), a taxpayer may choose to determine when physical work of a significant nature begins in accordance with the safe harbor rule provided in section 1.168(k)-1(b)(4)(iii)(B)(*2*). Under this safe harbor rule, physical work of a significant nature will not be considered to begin before the taxpayer incurs (in the case of an accrual basis taxpayer) or pays (in the case of a cash basis taxpayer) more than 10 percent of the total cost of the property (excluding the cost of any land and preliminary activities such as planning or designing, securing financing, exploring, or researching). When property is manufactured, constructed, or produced for the taxpayer by another person, this safe harbor rule must be satisfied by the taxpayer. A taxpayer chooses to apply section 1.168(k)-1(b)(4)(iii)(B)(*2*) by filing an income tax return for the placed-in-service year of the property that determines when physical work of a significant nature begins consistent with section 1.168(k)-1(b)(4)(iii)(B)(*2*).

Section 1.168(k)-1(b)(4)(iii)(C) provides the rules relating to components of self-constructed property. If such component is acquired by the taxpayer, the rules in section 1.168(k)-1(b)(4)(iii)(C)(*1*) apply to the acquired component. If the component is self-constructed, the rules in section 1.168(k)-1(b)(4)(iii)(C)(*2*) apply to the self-constructed component.

Section 1.168(k)-1(b)(4)(iii)(C)(*1*) provides that if a binding contract (as defined in section 1.168(k)-1(b)(4)(ii)) to acquire a component does not satisfy the requirements of section 1.168(k)-1(b)(4)(i), the component does not qualify for the 50-percent additional first year depreciation deduction. A binding contract to acquire one or more components of a larger self-constructed property will not preclude the larger self-constructed property from satisfying the acquisition rules in section 1.168(k)-1(b)(4)(iii)(A). Accordingly, the unadjusted depreciable basis of the larger self-constructed property that is eligible for the 50-percent additional first year depreciation deduction must not include the unadjusted depreciable basis of any component that does not satisfy the requirements of section 1.168(k)-1(b)(4)(i). If the manufacture, construction, or production of the larger self-constructed property begins before [January 1, 2008], the larger self-constructed property and any acquired components related to the larger self-constructed property do not qualify for the 50-percent additional first year depreciation deduction.

Section 1.168(k)-1(b)(4)(iii)(C)(*2*) provides that if the manufacture, construction, or production of a component does not satisfy the requirements of section 1.168(k)-1(b)(4)(iii)(A), the component does not qualify for the 50-percent additional first year depreciation deduction. However, if the manufacture, construction, or production of component does not satisfy the requirements of section 1.168(k)-1(b)(4)(iii)(A), but the manufacture, construction, or production of the larger self-constructed property satisfies the requirements of section 1.168(k)-1(b)(4)(iii)(A), the larger self-constructed property qualifies for the 50-percent additional first year depreciation deduction (assuming all other requirements in section 168(k)(2) are met). Accordingly, the unadjusted depreciable basis of the larger self-constructed property that is eligible for the 50-percent additional first year depreciation deduction must not include the unadjusted depreciable basis of any component that does not qualify for the 50-percent additional first year depreciation deduction. If the manufacture, construction, or production of the larger self-constructed property began before [January 1, 2008], the larger self-constructed property and any self-constructed components related to the larger self-constructed property do not qualify for the 50-percent additional first year depreciation deduction.

Section 168(k)(5) provides that in the case of qualified property acquired by the taxpayer (under rules similar to the rules of section 168(k)(2)(A)(ii) and (iii)) after September 8, 2010, and before January 1, 2012, and which is placed in service by the taxpayer before January 1, 2012 (January 1, 2013, in the case of property described in section 168(k)(2)(B) or (C)), a 100-percent additional first year depreciation deduction for the taxable year in which such qualified property is placed in service by the taxpayer is allowable.

Section 3.01 of Rev. Proc. 2011-26 provides that depreciable property is eligible for the 100-percent additional first year depreciation deduction if the property is qualified property (as defined in section 168(k)(2)) and also meets the additional requirements in section 3.02 of Rev. Proc. 2011-26. Further, it provides that for purposes of determining whether depreciable property is qualified property, rules similar to the rules in section 1.168(k)-1 for “qualified property” or for “30-percent additional first year depreciation deduction” apply.

Section 3.02(1) of Rev. Proc. 2011-26 provides that for purposes of section 168(k)(5), qualified property is eligible for the 100-percent additional first year depreciation deduction if the property meets all of the following requirements in the first taxable year in which the property is subject to depreciation by the taxpayer, whether or not depreciation deductions for that property are allowable:

(a) The taxpayer acquires the qualified property after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)). Solely for purposes of section 168(k)(5) and section 3.02(1)(a) of Rev. Proc. 2011-26, a taxpayer acquires the qualified property when the taxpayer pays or incurs the cost of the property. Qualified property that a taxpayer manufactures, constructs, or produces (as defined under section 1.168(k)-1(b)(4)(iii)(A) and modified by section 3.02(1)(a) of this revenue procedure solely for purposes of section 168(k)(5)) for use in its trade or business or for its production of income is acquired by the taxpayer for purposes of section 168(k)(5) and section 3.02(1)(a) of Rev. Proc. 2011-26 when the taxpayer begins constructing, manufacturing, or producing that property (as determined under section 1.168(k)-1(b)(4)(iii)(B)).

(b) The taxpayer places the qualified property in service after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)).

(c) The original use of the qualified property commences with the taxpayer after September 8, 2010.

Section 3.02(2)(a) of Rev. Proc. 2011-26 provides, in relevant part, that if a taxpayer manufactures, constructs, or produces qualified property for use by the taxpayer in its trade or business or for its production of income, rules similar to the self-constructed property rules in section 1.168(k)-1(b)(4)(iii) apply for determining whether this property meets the acquisition requirement of section 3.02(1)(a) of Rev. Proc. 2011-26.

Section 3.02(2)(b) of Rev. Proc. 2011-26, however, provides a limited exception to sections 1.168(k)-1(b)(4)(iii)(C)(*1*) and (*2*) for certain components of a larger self-constructed property solely for purposes of section 168(k)(5) and section 3.02(1)(a) of Rev. Proc. 2011-26. If before September 9, 2010, a taxpayer begins the manufacture, construction, or production of the larger self-constructed property that is qualified property for use in its trade or business or for its production of income, but this larger self-constructed property meets the requirements of sections 3.02(1)(b) and (c) of Rev. Proc. 2011-26, the taxpayer may elect to treat any acquired or self-constructed component of that larger self-constructed property as being eligible for the 100-percent additional first year depreciation deduction if the component is qualified property and is acquired or self-constructed by the taxpayer after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)). The taxpayer may make this election for one or more components that are described in section 3.02(2)(b) of Rev. Proc. 2011-26.

Section 461(a) provides, in part, that a deduction shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income.

Section 1.461-1(a)(2) provides, in part, that under an accrual method of accounting, a liability (as defined in section 1.446-1(c)(1)(ii)(B)) is incurred, and generally is taken into account for federal income tax purposes, in the taxable year in which all the 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. The first two requirements are commonly referred to as the all events test and the third requirement is called the economic performance requirement. *See also* section 1.446-1(c)(1)(ii)(A).

Sections 461(h) and 1.461-4(a) provide, in part, that in determining whether an amount has been incurred with respect to any item during the taxable year, the all events test shall not be treated as met any earlier than when economic performance with respect to such item has occurred.

Section 461(h)(2)(A)(i) and (ii) and section 1.461-4(d)(2)(i) provide that if the liability of the taxpayer arises out of the providing of services or property to the taxpayer by another person, economic performance occurs as services or property is provided.

Section 1.461-4(d)(6) provides the rules relating to the provision of services or property to the taxpayer for purposes of section 1.461-4(d). Section 1.461-4(d)(6)(iii) provides that a taxpayer is permitted to treat property as provided to the taxpayer when the property is delivered or accepted, or when title to the property passes. The method used by the taxpayer to determine when property is provided is a method of accounting that must comply with the rules of section 1.446-1(e). Thus, the method of determining when property is provided must be used consistently from year to year, and cannot be changed without the consent of the Commissioner of Internal Revenue.

Section 1.461-4(e) provides that in the case of interest, economic performance occurs as the interest cost economically accrues, in accordance with the principles of relevant provisions of the Code.

Section 461(h)(2)(D) provides that in the case of any other liability not specifically mentioned in section 461(h), economic performance occurs at the time determined by the Internal Revenue Service in regulations.

Section 1.461-4(g) provides a list of specifically enumerated items for which economic performance is satisfied by payment. Section 1.461-4(g)(7) provides that in the case of a taxpayer's liability for which economic performance rules are not otherwise provided elsewhere in the Code or other rules, economic performance occurs as the taxpayer makes payments in satisfaction of the liability. Section 1.461-4(g)(7) further states that its only application is if the liability in question is not covered by rules provided elsewhere under section 461.

Section 263A(a)(1) provides that in the case of any property to which section 263A applies, the direct costs of the property and the indirect costs properly allocable to the property shall be included in inventory costs (in the case of property that is inventory in the hands of the taxpayer) or shall be capitalized (in the case of other property).

Section 263A(b)(1) provides that, except as otherwise provided, section 263A shall apply to real or tangible personal property produced by the taxpayer. *See also* section 1.263A-1(a)(3)(i). For purposes of section 263A, section 263A(g)(1) provides that the term "produce" includes construct, build, install, manufacture, develop, or improve. *See also* section 1.263A-2(a)(1).

Section 263A(f)(1) provides that interest costs for property produced by the taxpayer is capitalized in case of interest costs which are paid or incurred during the production period, and allocable to property described in section 263A(b)(1) and which has a (i) long useful life, (ii) an estimated production period exceeding 2 years, or (iii) an estimated production period exceeding 1 year and a cost exceeding $1,000,000.

Section 263A(f)(4)(A) provides that property has a long useful life if such property is real property, or property with a class life of 20 years or more under section 168.

Section 263A(f)(4)(B) provides that the term "production period" means, when used with respect to any property, the period beginning on the date on which production of the property begins, and ending on the date on which the property is ready to be placed in service or is ready to be held for sale. *See also* section 1.263A-12.

Section 1.263A-8(a)(1) provides that capitalization of interest under the avoided cost method described in section 1.263A-9 is required with respect to the production of designated property described in section 1.263A-8(b).

Section 1.263A-8(a)(2) provides that interest that is capitalized under section 1.263A-8 is treated as a cost of the designated property and is recovered in accordance with section 1.263A-1(c)(4).

The term "designated property" is defined in section 1.263A-8(b)(1) as meaning, in general, any property that is produced and that is either (i) real property (as defined in section 1.263A-8(c)); or (ii) tangible personal property (as defined in section 1.263A-2(a)(2)) that meets any of the following criteria: (A) property with a class life of 20 years or more under section 168 but only if the property is not property described in section

1221(1) in the hands of the taxpayer or a related person; (B) property with an estimated production period (as defined in section 1.263A-12) exceeding 2 years; or (C) property with an estimated production period exceeding 1 year and an estimated cost of production exceeding $1,000,000.

Ruling Requests 1, 2, and 3

For purposes of applying the 50-percent additional first year depreciation deduction, the determination of whether property is a self-constructed property is made under section 1.168(k)-1(b)(4)(iii)(A).

In this case, Unit 1 and Unit 2 are constructed for Taxpayer by H under the Contract that Taxpayer represents was entered into before construction of Unit 1 and Unit 2. The Contract is dated Date2, which is prior to January 1, 2008. Taxpayer represents that the Contract is a written binding contract under the law of State1 and does not limit damages to an amount that is less than five percent of the Contract price.

However, the Contract was subject to a number of change orders and was amended by the Settlement Agreement in Year1, which is after 2007. The Settlement Agreement increased the total cost of the Facility by approximately 3.6 percent and extended the turnover dates for the Units. Neither the change orders nor the Settlement Agreement changed the location of the Facility or the nominal nameplate capacity of either Unit 1 or Unit 2. Section 1.168(k)-1(b)(4)(ii)(B) provides, in part, that a contract will continue to be binding if the parties make insubstantial changes in its terms and conditions. We find the 3.6-percent increase in the total cost of the Facility and the extended turnover dates to be insubstantial changes to the terms and conditions of the Contract. Accordingly, the Contract dated Date2 continues to be binding for purposes of section 1.168(k)-1(b)(4).

Consequently, Unit 1 and Unit 2 are self-constructed property for purposes of the 50-percent additional first year depreciation deduction provided by section 168(k)(1). Because Unit 1 and Unit 2 are self-constructed property, they are acquired by Taxpayer when Taxpayer begins construction of each respective Unit for purposes of the acquisition requirement of section 168(k)(2)(A)(iii), section 168(k)(2)(E)(i), and section 1.168(k)-1(b)(4)(i).

For self-constructed property, the acquisition requirement for purposes of the 50-percent additional first year depreciation deduction is treated as met if Taxpayer begins manufacturing, constructing, or producing the property after December 31, 2007, and before January 1, 2013 (before January 1, 2014, in the case of qualified property described in section 168(k)(2)(B) or (C)).

For purposes of the 50-percent additional first year depreciation deduction, manufacture, construction, or production of property begins when physical work of a significant nature begins. To make this determination, the taxpayer may choose to apply the 10-percent safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*).

Under this safe harbor, physical work of a significant nature will not be considered to begin before an accrual basis taxpayer incurs more than 10 percent of the total cost of the property (excluding the cost of any land and preliminary activities). Because the term "incurred" is neither defined nor given any special meaning in section 168(k) or its underlying regulations or legislative history, the determination of when an accrual basis taxpayer has incurred more than 10 percent of the total cost of the property is made using the all events test and economic performance requirement of section 461, which specifically governs the timing of the deductions, costs, and expenses at issue.

If Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(*2*) for Unit 1 and Unit 2, such rule applies for determining when Taxpayer began construction of Unit 1 and Unit 2. Under this safe harbor rule, Taxpayer, an accrual basis taxpayer, determines when it incurred more than 10 percent of the total cost of each Unit by applying the all events test and economic performance requirement of section 461.

In the case of Unit 1 and Unit 2, Taxpayer represents that each Unit are phases of a turnkey contract where turnover, as defined under the Contract, occurs when the contractor (H) has completed all work required for turnover and when the care, custody and control and risk of loss for each phase has transferred to Taxpayer. Costs associated with the provision of property are incurred when all the events have occurred that establish the fact of liability, the amount of the liability can be determined with reasonable accuracy, and the property has been provided to Taxpayer. In this case, Taxpayer represents that, for its initial federal income tax return, Taxpayer is adopting a method of accounting for purposes of section 1.461-4(d)(6)(iii) that will treat property as provided to Taxpayer when the property is accepted by Taxpayer. Thus, the all events test is satisfied and economic performance has occurred when the turnover, as defined under the Contract, occurs. At that time, the liability is fixed, the amount of the liability has been determined with reasonable accuracy, and risk of loss has passed to Taxpayer.

Taxpayer represents that turnover, as defined under the Contract, of Unit 1 occurred on Date7, and of Unit 2 occurred on Date8. Thus, no costs attributable to the Contract were incurred by Taxpayer before Date7, for Unit 1, and before Date8, for Unit 2.

Ruling Requests 4 and 5

However, in addition to the costs attributable to the Contract, Taxpayer and its affiliates incurred a small amount of other costs for the construction of the Facility for items like permitting, project development, project design, engineering, preconstruction,

construction management, and troubleshooting costs. Further, in accordance with section 263A(f)(1) and section 1.263A-8(a), Taxpayer capitalized interest during the production periods of Unit 1 and Unit 2. Pursuant to section 1.263A-8(a)(2), the interest that Taxpayer capitalized under section 1.263A-8 to Unit 1 and Unit 2 is treated as a cost of Unit 1 and Unit 2, respectively.

For purposes of the safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(2), the total cost of the property excludes the cost of any land and preliminary activities such as planning or designing, securing financing, exploring, or researching. We do not consider interest capitalized under section 263A(f) to be a preliminary activity. Accordingly, for purposes of the safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(2), the total cost of the property includes any interest capitalized under section 263A(f) to that property. In the case of interest, section 1.461-4(e) provides that economic performance occurs as the interest cost economically accrues, in accordance with the principles of relevant provisions of the Code.

Taxpayer represents that with respect to Unit 1, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of January 1, 2008, were 10 percent or less of the final tax basis of Unit 1 as of the original placed-in-service date. Taxpayer represents that the prior sentence is not altered even if one accrues capitalized interest on costs incurred by Taxpayer and payments made to H through January 1, 2008.

Taxpayer represents that with respect to Unit 2, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of January 1, 2008, were 10 percent or less of the final tax basis of Unit 2 as of the original placed-in-service date. Taxpayer represents that the prior sentence is not altered even if one accrues capitalized interest on costs incurred by Taxpayer and payments made to H through January 1, 2008.

Therefore, if Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(2) for Unit 1 and Unit 2, Taxpayer began construction of Unit 1 and Unit 2 after December 31, 2007.

Ruling Request 6

To qualify for the 50-percent additional first year depreciation under section 168(k)(1), property must be “qualified property” under section 168(k)(2). Under section 168(k)(2)(A), qualified property is, in general, property (i) among other things, to which section 168 applies with a recovery period of 20 years or less, (ii) the original use of which commences with the taxpayer after December 31, 2007, (iii) that is acquired by the taxpayer after December 31, 2007, and before January 1, 2013, but only if no written binding contract for the acquisition was in effect before January 1, 2008, or that is acquired by the taxpayer pursuant to a written binding contract which was entered into after December 31, 2007, and before January 1, 2013, and (iv) that is placed in service by the taxpayer before January 1, 2013, or in the case of property described in section 168(k)(2)(B) or (C), before January 1, 2014.

In the case of self-constructed property, section 168(k)(2)(E)(i) (as amended by the TRUIRJCA) provides that the requirements of section 168(k)(2)(A)(iii) shall be treated as met if the taxpayer begins manufacturing, constructing, or producing the property after December 31, 2007, and before January 1, 2013.

However, property is not qualified property if the property is required to be depreciated under the alternative depreciation system of section 168(g) pursuant to section 168(g)(1)(A) through (D) or other provisions of the Code. Section 168(k)(2)(D)(i) and section 1.168(k)-1(b)(2)(ii)(A)(*2*).

In the case of Unit 1, Taxpayer represents that Unit 1 is described in asset class 49.13 of Rev. Proc. 87-56. Taxpayer also represents that Unit 1 may include a small amount of transmission property that is described in asset class 49.14 of Rev. Proc. 87-56. Property included in asset class 49.13 or asset class 49.14 is 20-year property. Thus, for purposes of section 168(k)(2)(A)(i), the recovery period of Unit 1 is 20 years. Further, section 168 applies to Unit 1. Moreover, Taxpayer represents that the property subject to this ruling request with respect to Unit 1 is not required to be depreciated under the alternative depreciation system of section 168(g).

Taxpayer represents that the original use of Unit 1 commenced with Taxpayer and Unit 1 was originally placed in service on Date7, which is after December 31, 2007, and before September 9, 2010. Thus, the original use of Unit 1 commenced with Taxpayer after December 31, 2007, and Taxpayer placed in service Unit 1 after December 31, 2007, and before September 9, 2010.

Further, as previously discussed, Unit 1 is self-constructed property and, if Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(*2*) for Unit 1, construction of Unit 1 began after December 31, 2007. Consequently, if Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(*2*) for Unit 1, Unit 1 satisfies the requirements of section 168(k)(2)(E)(i) and, therefore, the acquisition requirement in section 168(k)(2)(A)(iii) is treated as met.

Therefore, the section 1245 property of Unit 1 meets all of the requirements to be qualified property under section 168(k)(2)(A) and is eligible for the 50-percent additional first year depreciation deduction under section 168(k)(1) (assuming section 168(k)(2)(D)(ii) and (iii), section 168(k)(2)(E)(ii)-(iv), and section 168(k)(4) do not apply).

Ruling Request 7

In the case of Unit 2, Taxpayer represents that Unit 2 is described in asset class 49.13 of Rev. Proc. 87-56. Taxpayer also represents that Unit 2 may include a small amount of transmission property that is described in asset class 49.14 of Rev. Proc. 87-56. Property included in asset class 49.13 or asset class 49.14 is 20-year property. Thus, for purposes of section 168(k)(2)(A)(i), the recovery period of Unit 2 is 20 years. Further, section 168 applies to Unit 2. Moreover, Taxpayer represents that the property subject to this ruling request with respect to Unit 2 is not required to be depreciated under the alternative depreciation system of section 168(g).

Taxpayer represents that the original use of Unit 2 commenced with Taxpayer and Unit 2 was originally placed in service on Date8, which is after September 8, 2010, and before January 1, 2012. Thus, the original use of Unit 2 commenced with Taxpayer after September 8, 2010, and Taxpayer placed in service Unit 2 after September 8, 2010, and before January 1, 2012.

Further, as previously discussed, Unit 2 is self-constructed property and, if Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(*2*) for Unit 2, construction of Unit 2 began after December 31, 2007. Consequently, if Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(*2*) for Unit 2, Unit 2 satisfies the requirements of section 168(k)(2)(E)(i) and, therefore, the acquisition requirement in section 168(k)(2)(A)(iii) is treated as met.

Therefore, the section 1245 property of Unit 2 meets all of the requirements to be qualified property under section 168(k)(2)(A) and is eligible for the 50-percent additional first year depreciation deduction under section 168(k)(1) (assuming section 168(k)(2)(D)(ii) and (iii), section 168(k)(2)(E)(ii)-(iv), and section 168(k)(4) do not apply).

If Unit 2 and all of its components are qualified property, Taxpayer intends to determine whether any component of Unit 2 is eligible for the 100-percent additional first year depreciation by applying the limited election in section 3.02(2)(b) of Rev. Proc. 2011-26.

That election applies to a taxpayer that began manufacturing, constructing, or producing a larger self-constructed property that is qualified property before September 9, 2010, but the taxpayer placed this larger self-constructed property in service after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)) and the original use of the larger self-constructed property commenced with the taxpayer after September 8, 2010. In such a case, the taxpayer may elect to treat any acquired or self-constructed component of that larger self-constructed property as being eligible for the 100-percent additional first year depreciation deduction if the component is qualified property and is acquired or self-constructed by the taxpayer after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)).

Solely for purposes of section 168(k)(5) and section 3.02(1)(a) of Rev. Proc. 2011-26, section 3.02(1)(a) of this revenue procedure provides that a taxpayer acquires the qualified property when the taxpayer pays or incurs the cost of the property. The term "pays or incurs" means pays or incurs within the meaning of sections 1.461-1(a)(1) and (2). Accordingly, an accrual basis taxpayer acquires qualified property solely for purposes of section 168(k)(5) when the accrual basis taxpayer incurs the cost of the property and a cash basis taxpayer acquires qualified property solely for purposes of section 168(k)(5) when the cash basis taxpayer pays the cost of the property.

If a taxpayer manufactures, constructs, or produces qualified property for use in its trade or business, section 3.02(1)(a) of Rev. Proc. 2011-26 also provides that such property is acquired by the taxpayer for purposes of section 168(k)(5) and section 3.02(1)(a) of this revenue procedure when the taxpayer begins constructing, manufacturing, or producing that property as determined under section 1.168(k)-1(b)(4)(iii)(B).

Under the limited election of section 3.02(2)(b) of Rev. Proc. 2011-26, the component must be qualified property and must be acquired or self-constructed by the taxpayer after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)). The dates of this acquisition requirement are the same dates as in the acquisition requirements in section 3.02(1)(a) of Rev. Proc. 2011-26. Although the acquisition requirements in section 3.02(1)(a) of Rev. Proc. 2011-26 do not specifically incorporate the limited election under section 3.02(2)(b) of Rev. Proc. 2011-26, the Service intended to apply such acquisition requirements also for purposes of section 3.02(2)(b) of Rev. Proc. 2011-26 for any acquired or self-constructed component of the larger self-constructed property described in section 3.02(2)(b) of Rev. Proc. 2011-26. Thus, for purposes of section 3.02(2)(b) of Rev. Proc. 2011-26, a taxpayer may elect to treat any acquired component of the larger self-constructed property described in section 3.02(2)(b) of Rev. Proc. 2011-26 as being eligible for the 100-percent additional first year depreciation deduction if the acquired component is qualified property and if the taxpayer incurs (in the case of an accrual basis taxpayer) or pays (in the case of a cash basis taxpayer) the cost of the acquired component after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of property described in section 168(k)(2)(B) or (C)).

Further, for purposes of section 3.02(2)(b) of Rev. Proc. 2011-26, a taxpayer may elect to treat any self-constructed component of the larger self-constructed property described in section 3.02(2)(b) of Rev. Proc. 2011-26 as being eligible for the 100-percent additional first year depreciation deduction if the self-constructed component is qualified property and if the taxpayer begins manufacturing, constructing, or producing the component (as determined under section 1.168(k)-1(b)(4)(iii)(B)) after September 8, 2010, and before January 1, 2012 (before January 1, 2013, in the case of property described in section 168(k)(2)(B) or (C)). Pursuant to section 1.168(k)-1(b)(4)(iii)(B)(*1*), manufacture, construction, or production of property begins when physical work of a significant nature begins. To make this determination, a taxpayer may choose to apply the 10-percent safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*). Under this safe harbor rule, physical work of a significant nature will not be considered to begin before an accrual basis taxpayer incurs more than 10 percent of the total cost of the property (excluding the cost of any land and preliminary activities).

As we previously discussed under Ruling Requests 1, 2, and 3, the term "incurred" is neither defined nor given any special meaning in section 168(k) or its underlying regulations or legislative history. Such term also is not defined nor given any special meaning in Rev. Proc. 2011-26 for purposes of the 10-percent safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*). Accordingly, our conclusion reached under Ruling Requests 1, 2, and 3 also applies for purposes of section 168(k)(5) and sections 3.02(1)(a) and 3.02(2)(b) of Rev. Proc. 2011-26. That is, the determination of when an accrual basis taxpayer has incurred the cost of the acquired component is made using the all events test and economic performance requirement of section 461 and, for purposes of the safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*), has incurred more than 10 percent of the total cost of a self-constructed component is made using the all events test and economic performance requirement of section 461.

In the case of Unit 2, Taxpayer represents that, assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of September 9, 2010, excluding any capitalized interest, were 10 percent or less of the final tax basis of Unit 2 as of the original placed in service date. Further, Taxpayer's representative, J, stated that assuming that no costs were incurred with respect to the Contract until turnover, the costs that were incurred as of September 9, 2010, including any capitalized interest, were probably more than 10 percent of the final tax basis of Unit 2 as of the original placed in service date. As previously discussed under Ruling Requests 4 and 5, the total cost of the property includes any interest capitalized under section 263A(f) to that property for purposes of the safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*). Thus, if Taxpayer chooses the safe harbor rule of section 1.168(k)-1(b)(4)(iii)(B)(*2*) for Unit 2, the construction of Unit 2 began after December 31, 2007, and before September 9, 2010. Consequently, Unit 2 is not eligible for the 100-percent additional first year depreciation deduction provided under section 168(k)(5).

However, as previously discussed under this Ruling Request 7, the original use of Unit 2 commenced with Taxpayer after September 8, 2010, and Taxpayer placed in service Unit 2 after September 8, 2010, and before January 1, 2012. Consequently, Unit 2, the larger self-constructed property, is described in section 3.02(2)(b) of Rev. Proc. 2011-26. Thus, Taxpayer may elect to treat any acquired or self-constructed component of that larger self-constructed property as being eligible for the 100-percent additional first year depreciation deduction if the component is qualified property and is acquired or self-constructed by Taxpayer after September 8, 2010, and before January

1, 2012 (before January 1, 2013, in the case of qualified property described in section 168(k)(2)(B) or (C)). Taxpayer may make this election for one or more components that are described in section 3.02(2)(b) of Rev. Proc. 2011-26.

CONCLUSION

Based solely on Taxpayer's representations and the relevant law and analysis set forth above, we conclude that:

1. Unit 1 and Unit 2 are each self-constructed property as defined in section 1.168(k)-1(b)(4)(iii)(A).

2. The fact that Taxpayer and H entered into the Contract prior to January 1, 2008, does not prevent Unit 1 and Unit 2 from meeting the acquisition requirements in sections 168(k)(2)(A)(iii) and (E)(i).

3. For purposes of determining for each of the Units when physical work of a significant nature begins under the 10-percent safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*), no costs are incurred by Taxpayer under the Contract until turnover (as defined in the Contract) has occurred. As a result, no costs attributable to the Contract were incurred before (a) Date7, in the case of Unit 1, when turnover of Unit 1 occurred, and (b) Date8, in the case of Unit 2, when turnover of Unit 2 occurred.

4. For purposes of section 1.168(k)-1(b)(4)(iii)(B)(*2*), construction of Unit 1 began after December 31, 2007 (if Taxpayer chooses the 10-percent safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*)).

5. For purposes of section 1.168(k)-1(b)(4)(iii)(B)(*2*), construction of Unit 2 began after December 31, 2007 (if Taxpayer chooses the 10-percent safe harbor rule under section 1.168(k)-1(b)(4)(iii)(B)(*2*)).

6. The section 1245 property at Unit 1 qualifies for the 50-percent additional first year depreciation deduction under section 168(k)(1) (assuming section 168(k)(2)(D)(ii) and (iii), section 168(k)(2)(E)(ii)-(iv), and section 168(k)(4) do not apply).

7. The section 1245 property at Unit 2 qualifies for the 50-percent additional first year depreciation deduction under section 168(k)(1) (assuming section 168(k)(2)(D)(ii) and (iii), section 168(k)(2)(E)(ii)-(iv), and section 168(k)(4) do not apply). If a proper election is made pursuant to section 3.02(2)(b) of Rev. Proc. 2011-26, any components of Unit 2 acquired or self-constructed by Taxpayer after September 8, 2010, may qualify for the 100-percent additional first year depreciation deduction under section 168(k)(5), provided that the component(s) is qualified property as defined in section 168(k)(2).

Except as specifically set forth above, no opinion is expressed or implied concerning the tax consequences of the facts described above under any other provisions of the Code (including other subsections of section 168). Specifically, no opinion is expressed or implied on: (i) whether the Contract is a binding contract under the law of State1 or any other State; (ii) the original-use-date and the placed-in-service date of Unit 1 and Unit 2; (iii) the asset classification under Rev. Proc. 87-56 of Unit 1 and Unit 2; (iv) whether the lease of the Facility to D is a lease for Federal income tax purposes; or (v) whether Taxpayer's method of capitalizing interest is in accordance with section 263A(f) and the regulations thereunder. Taxpayer's interest capitalization method of accounting includes, but is not limited to, when production starts and ends, what expenses are included in accumulated production expenditures, measurement periods, etc.

In accordance with the power of attorney, we are sending a copy of this letter to Taxpayer's authorized representatives. We are also sending a copy of this letter to the appropriate operating division director.

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

Sincerely,

Kathleen Reed

Kathleen Reed
Branch Chief, Branch 7
Office of Associate Chief Counsel
(Income Tax and Accounting)