Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:ITA:7
PLR-128349-11
Date:
January 03, 2012

Re: Request for Private Letter Ruling Regarding § 167

Legend

Taxpayer =

A =

B =

C =

D =

E =

F =

G =

H =

I =

J =

Dear :

This letter responds to a letter dated June 30, 2011, submitted by Taxpayer requesting a letter ruling on whether any of the consideration paid to acquire the assets of a wind generation trade or business is allocated to facility-specific power purchase agreements as separate assets.

FACTS

Taxpayer represents that the facts are as follows:

Taxpayer is an electric company. Through its subsidiaries and affiliates, Taxpayer generates, markets, transmits, and distributes electricity.

On A, Taxpayer, using a chain of entities that are disregarded as separate from their owners for federal income tax purposes ("disregarded entities"), acquired all of the membership interests in B, an unrelated party (the "Transaction"). At the time of the Transaction, B was a holding company whose assets consisted of all of the membership interests of C disregarded entities and interests in D partnerships. Each of these E entities owned and operated one or more wind energy facilities or was in the process of constructing a wind energy facility that it intended to own and operate. As of the date of the Transaction, all of the D partnerships had in place elections under section 754 of the Internal Revenue Code.

Each wind energy facility consisted of various items of tangible property including land, wind turbines, towers, pads, transformers, on-site power collection systems, monitoring and meteorological equipment and site improvements such as roadways and fencing.

Prior to the date of the Transaction, the E entities had entered into approximately F separate power purchase agreements ("PPAs"), pursuant to which the selling entity committed to sell some or all of the output of its wind facilities to a counterparty in accordance with the terms and conditions of the PPA. While the F PPAs are not identical in every respect, they do share certain relevant characteristics. The key shared characteristic is that all of the PPAs are facility-specific. That is, such PPAs obligate the producer of the electricity generated at a specific wind energy facility to sell, and the buyer to purchase, a specified amount of the output of that specific wind facility. Under each of these PPAs, there are no circumstances under which the producer can produce or obtain capacity, energy, or environmental attributes required to fulfill its obligations under the PPA from sources other than the specific wind energy facility designated in the PPA. A transfer of a PPA without a transfer of the related wind energy facility would leave the transferee with no means of satisfying the PPA.

At the time of the Transaction, a number of the PPAs still had significant periods remaining. Due to fluctuations in the price of energy since the inception of many of these PPAs, the pricing they incorporated had, by the time of the Transaction, become favorable by reference to the market price of power on that date. In other words, the price that Taxpayer is entitled to charge under the PPAs is greater than the market price of power on the date of the Transaction.

Taxpayer engaged G to value the assets it purchased in the Transaction for financial reporting purposes. As part of that process, G evaluated all the acquired property, plant, and equipment, including facilities under construction, owned by each of the E entities, as well as each of the F PPAs. Based on its analysis, G determined a total value of approximately $H million to the property, plant, and equipment, and approximately $I million to the PPAs.

There were no related parties (related buyer and seller) that were parties to the same PPA at the time prior to, on, or after the date of the Transaction.

Taxpayer provided a copy of a Wind Generation Purchase Agreement ("Sample PPA") that is similar in nature to each of the PPAs subject to Taxpayer's letter ruling request. Under the terms of the Sample PPA, the producer of the electricity generated at a specific wind energy facility agreed to sell all of: (1) the output potential of that wind energy facility (the "Capacity"); (2) the actual number of megawatt-hours (MWh) generated by that wind energy facility during the term of the Sample PPA less any generating output in MWh used by the producer to operate the wind energy facility and distribution losses as measured by meters installed (the "Net Energy"); and (3) all attributes (environmental or otherwise) that are created or otherwise arise from that wind energy facility's generation of electricity using wind as a fuel, including but not limited to, tags, certificates, or similar products or rights associated with wind as a "green" or "renewable" electric generation resource (the "Green Tags"). Further, under the terms of the Sample PPA, the price used as the basis for determining payments by the buyer to the producer for the Capacity, Net Energy, and Green Tags of the wind energy facility is $J per MWh during the term of the Sample PPA (the "Guaranteed Price").

While many of the PPAs subject to Taxpayer's letter ruling request require the producer to sell, and the buyer to purchase, all of the electricity produced by a specific wind energy facility during the term of the PPA, a few of the subject PPAs require the producer to sell, and the buyer to purchase, a specified cap amount of the specific wind energy facility's output, which, in a given year, may be less than all of that facility's output. A PPA of this type may provide for a pricing adjustment to account for market pricing for the output delivered in excess of the cap amount. Under both types of PPAs, Taxpayer can satisfy its obligations under the PPAs only with the power produced at the specific wind energy facility designated in the PPA.

RULING REQUESTED

Taxpayer requests the Internal Revenue Service issue the following ruling:

Where Taxpayer acquired wind energy facilities subject to facility-specific PPAs, no portion of its purchase price shall be allocated to the PPAs and the purchase price of such wind energy facilities that is attributed to such PPAs shall be taken into account in determining the adjusted basis of the wind energy facilities.

LAW AND ANALYSIS

Section 167(a) provides that there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear, and obsolescence of property used in the trade or business, or in the production of income.

Section 167(c) provides the rules for determining basis for depreciation purposes. Pursuant to section 167(c)(1), the basis on which exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property is the adjusted basis provided in section 1011, for the purpose of determining the gain on the sale or other disposition of such property. If any property is acquired subject to a lease, section 167(c)(2) provides that (A) no portion of the adjusted basis is allocated to the leasehold interest, and (B) the entire adjusted basis is taken into account in determining the depreciation deduction (if any) with respect to the property subject to the lease.

In this case, Taxpayer acquired wind energy facilities and certain PPAs from an unrelated party. Taxpayer represents that each of the PPAs subject to its letter ruling request require the producer of the electricity generated by a specific wind energy facility to sell, and the buyer to purchase, all, or a specified cap amount, of the output of that specific facility for a specified price for a specified term of years. In the cases where the PPA requires the producer to sell, and the buyer to purchase, a specified cap amount of a specific wind energy's facility output, the PPA may provide a pricing adjustment to the specified price when output is delivered in excess of the cap amount. Taxpayer also represents that under the terms of each PPA subject to its letter ruling request, there are no circumstances under which the producer can produce or obtain capacity, energy, or environmental attributes required to fulfill its obligations under the PPA from sources other than the specific wind energy facility designated in the PPA. Moreover, Taxpayer represents that if a facility-specific PPA at issue is transferred to another party without a transfer of the related wind energy facility to that same party, the transferee would have no means of satisfying its obligations under the PPA. All of these representations are material representations. In such a case, we believe the specific-facility PPA should not be treated as an asset separate from the wind energy facility subject to such PPA. Accordingly, where Taxpayer acquired a wind energy facility subject to a facility-specific PPA at issue, the portion of the purchase price of the wind

energy facility that is attributable to that facility-specific PPA is taken into account as part of the basis of the wind energy facility for depreciation purposes.

CONCLUSION

Based solely on Taxpayer's representations and the relevant law and analysis set forth above, we conclude that where Taxpayer acquired wind energy facilities subject to facility-specific PPAs, no portion of its purchase price shall be allocated to the PPAs and the purchase price of such wind energy facilities that is attributed to such PPAs shall be taken into account in determining the adjusted basis of the wind energy facilities.

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 167).

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

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.

Sincerely,

Kathleen Reed

KATHLEEN REED
Chief, Branch 7
Office of Associate Chief Counsel
(Income Tax and Accounting)

Enclosures (2):
copy of this letter
copy for section 6110 purposes