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Person To Contact:

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Telephone Number:

Refer Reply To:

CC:ITA:B01

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Date:

December 08, 2015

Legend

Taxpayer	=
Parent	=
Commission	=
A	=
B	=
Plant	=
Year 1	=
Year 2	=
Year 3	=
Year 4	=
Court	=

Dear :

This letter responds to your request for a letter ruling that was submitted on behalf of Taxpayer by your authorized representative. Taxpayer has requested the following two rulings: (1) Taxpayer is entitled to a loss deduction in Year 1 pursuant to section 165(a) of the Internal Revenue Code for costs related to the construction and abandonment of an Independent Spent Fuel Storage Installation (“ISFSI”), which loss has not been “compensated for by insurance or otherwise”; and (2) the ISFSI costs are “otherwise deductible” nuclear decommissioning costs within the meaning of section 1.468A-1(b)(6) of the Income Tax Regulations.

FACTS

Taxpayer represents the facts and information related to its request for rulings as follows:

Taxpayer, a corporation, is a wholly-owned subsidiary of Parent. Parent and its affiliated group of corporations, including Taxpayer, electronically file a consolidated federal income tax return on a calendar year basis using the accrual method of accounting.

Taxpayer is a public utility regulated by the Commission. It owns a A percent interest in and is responsible for B percent of the decommissioning liability for Plant. Plant is a nuclear generating facility that permanently ceased operations in Year 2. As a result, and pursuant to Nuclear Regulatory Commission (“NRC”) regulations, the operating licenses for Plant no longer authorize its operation or the emplacement or retention of fuel in Plant’s reactors’ vessels.

Taxpayer established a qualified nuclear decommissioning fund (“Fund”) for Plant and has made annual deductible contributions to the Fund for taxable years Year 3 through the first quarter of Year 1 pursuant to a series of schedules of ruling amounts approved by the Service. The ruling amounts approved by the Service are based on estimated nuclear decommissioning costs approved by the Commission in determining rates for Taxpayer’s customers (“ratepayers”). The estimated costs are based on studies that looked at the cost to construct, operate and decommission an on-site ISFSI for Plant.

The Nuclear Waste Policy Act of 1982 states that the United States Government is responsible for the permanent disposal of high-level radioactive waste and spent nuclear fuel. Taxpayer, as a condition of its NRC license, entered into contracts with the United States Department of Energy (“DOE”) to provide for the disposal of its nuclear waste.

Spent nuclear fuel is a highly radioactive byproduct of nuclear power generation that must cool in a spent fuel pool for three to five years before it is moved to either temporary or permanent dry storage. After the cooling period, Taxpayer moves the nuclear waste to dry storage in an ISFSI. Taxpayer is responsible for the storage and related costs of nuclear waste until it is accepted by the DOE.

By the end of July, Year 2, all fuel was removed from Plant and placed in interim wet storage. Taxpayer began incurring costs for construction of an ISFSI at Plant in Year 4. The ISFSI is primarily underground and consists of vertical modules embedded in concrete on a concrete pad. When spent fuel is removed from the wet storage pool, it is placed permanently in canisters that are lowered into the vertical modules and covered by a steel and concrete lid. Taxpayer currently incurs, and will incur additional costs to expand the ISFSI so that all nuclear waste can be safely and securely held in dry storage pending transfer to the DOE.

The DOE has not yet constructed a permanent repository for nuclear waste and for this reason will not accept Taxpayer's nuclear waste for disposal. Taxpayer has filed complaints against the DOE for breach of contract in the Court for costs incurred by Taxpayer from Year 4 to Year 2. Taxpayer has been awarded damages for costs incurred during several years at issue. Litigation remains pending for other years and additional litigation is planned for current and future years.

Taxpayer recovers ISFSI costs (and other decommissioning costs) from ratepayers through ratemaking mechanisms approved by the Commission. Any decommissioning costs paid for by ratepayers that are not incurred by the Taxpayer or are not deemed prudent and reasonable by the Commission are refunded to ratepayers. Through regulatory rulings, the Commission has required Taxpayer to refund all current and future proceeds from the DOE litigation to ratepayers. The DOE litigation proceeds go to a specified Commission approved interest-bearing account and are refunded to ratepayers, with interest, through ratemaking mechanisms. Taxpayer has acknowledged that it is not entitled to DOE litigation proceeds (except reimbursement of reasonable litigation costs) and will refund recovered amounts as prescribed by the Commission.

LAW

Section 468A(a) of the Code allows taxpayers with a qualifying interest in a nuclear power plant to currently deduct the future costs of decommissioning the nuclear power plant by making contributions to a Fund prior to when economic performance occurs.

Section 468A(c)(1) of the Code generally requires the taxpayer to include in gross income amounts that are distributed from a Fund. In addition to any deduction under section 468A(a) for contributions to a Fund, section 468A(c)(2) recognizes that such taxpayer may deduct otherwise deductible nuclear decommissioning costs.

Section 1.468A-1(b)(6) of the regulations states that "nuclear decommissioning costs" means all otherwise deductible expenses to be incurred in connection with the entombment, decontamination, dismantlement, removal and disposal of the structures, systems and components of a nuclear power plant, whether that nuclear power plant will continue to produce electric energy or has permanently ceased to produce electric energy. Such term includes all otherwise deductible expenses to be incurred in connection with the preparation for decommissioning, such as engineering and other planning expenses, and all otherwise deductible expenses to be incurred with respect to the plant after the actual decommissioning occurs, such as physical security and radiation monitoring expenses. Such term also includes costs incurred in connection with the construction, operation, and ultimate decommissioning of a facility used solely to store, pending acceptance by the government for permanent storage or disposal, spent nuclear fuel generated by the nuclear power plant or plants located on the same site as the storage facility. Such term does not include otherwise deductible expenses

to be incurred in connection with the disposal of spent nuclear fuel under the Nuclear Waste Policy Act of 1982 (Pub.L. 97-425). An expense is otherwise deductible for purposes of this paragraph (b)(6) if it would be deductible under chapter 1 of the Internal Revenue Code without regard to section 280B.

Section 165 of the Code provides that there shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

Section 1.165-1(b) of the regulations provides that to be allowable as a deduction under section 165(a), a loss must be evidenced by closed and completed transactions, fixed by identifiable events, and actually sustained during the taxable year.

For a loss to qualify as a deductible abandonment loss, the taxpayer must show an intention to abandon the asset and an affirmative act of abandonment. In the case of physical abandonment, the intent of the taxpayer must be irrevocably to discard the asset so that it will neither be used again nor retrieved for sale, exchange or other disposition. A taxpayer need not relinquish title in all cases to establish abandonment. See Treas. Reg. §§ 1.165-2(c), 1.167(a)-8; Rev. Rul. 2004-58, 2004-1 C.B. 1043.

Section 1.165-1(d)(2)(i) of the regulations provides that, if an event occurs which may result in a loss and, in the year of the event, there exists a claim for reimbursement with respect to which there is a reasonable prospect of recovery, no portion of the loss with respect to which reimbursement may be received is sustained until it can be ascertained with reasonable certainty whether or not such reimbursement will be received.

ANALYSIS

The abandonment of real property interests where ownership has not been transferred has been addressed in a variety of circumstances. An abandonment was found where the taxpayer filled and sealed a water well excavation in Rev. Rul. 56-599, 1956-2 C.B. 122; dismantled an asphalt plant, moved it to another location and did not reassemble it, Seminole Rock & Sand Co. v. Commissioner, 19 T.C. 259 (1952), acq., 1953-1 C.B. 6; stopped working on a mine, reduced the work force and budget to maintain it, sold the mine equipment for salvage, decided to abandon the mine by vote of board of directors, and wrote the mine off the company books, A.J. Industries, Inc. v. United States, 503 F.2d 660 (9th Cir. 1974); and locked and boarded hotel, placed barricades around it, cut off utilities, terminated insurance, discontinued maintenance, and made no efforts to sell or lease it. Hanover v. Commissioner, T.C. Memo. 1979-332.

A nuclear generating facility is a heavily regulated asset, and one which Taxpayer cannot simply walk away from, board up, or dismantle. Taxpayer has taken affirmative, overt actions necessary to abandon the Plant. When an ISFSI is constructed after a nuclear facility has ceased operation, it is an integral component of the facility itself, and construction of the ISFSI is a necessary step in the process of decommissioning the

abandoned facility.

The ISFSI may be considered abandoned only as it is irrevocably committed to the process of decommissioning the abandoned facility. Costs related to an asset that can be sold or used for another purpose cannot qualify, even though the taxpayer intends to use it in the decommissioning process. The concrete pad and other structural components of the ISFSI are irrevocably committed to the decommissioning process as costs are incurred to build the ISFSI. The canisters are irrevocably committed to the decommissioning process as they are filled with spent fuel and placed in the ISFSI.

Based on the above, it is held that Taxpayer sustained an abandonment loss within the meaning of section 165(a) of the Internal Revenue Code. At issue, however, is whether Taxpayer is precluded from claiming the deduction because it has a claim for reimbursement with respect to which there is a reasonable prospect of recovery.

Taxpayer is engaged in litigation with the DOE for breach of contract related to DOE's refusal to accept Taxpayer's nuclear waste for permanent disposal, and has prevailed with respect to claims for certain years. Taxpayer represents, however, that Taxpayer has no legal right to the DOE litigation proceeds, is not in actual or constructive receipt of the proceeds, and is legally obligated to refund all such proceeds to its ratepayers, with interest, as prescribed by the Commission. Regulatory documents provided support this representation. In Year 1, therefore, Taxpayer has no claim for reimbursement with respect to which there is a reasonable prospect of recovery and is entitled to a deduction in Year 1 pursuant to section 165(a) for the costs associated with the construction and decommissioning of the ISFSI.

Under section 468A and the regulations thereunder, to be included within the ambit of nuclear decommissioning costs, all costs must be "otherwise deductible." Section 468A does not provide an independent basis for the deduction of any amounts except for those amounts contributed to a qualified fund as provided in section 468A(a). Those costs incurred in connection with the construction, operation, and ultimate decommissioning of a facility used solely to store, pending acceptance by the government for permanent storage or disposal, spent nuclear fuel generated by the nuclear power plant or plants located on the same site as the storage facility must also be "otherwise deductible."

As discussed above, the costs associated with the construction and decommissioning of the ISFSI are otherwise deductible under section 165. Accordingly, we rule that these costs constitute decommissioning costs within the meaning of section 1.468A-1(b)(6) of the regulations and, to the extent they are used for the purposes specified in section 1.468A-1(b)(6), may be paid out of the Funds.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

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

Sincerely,

Andrew M. Irving
Senior Counsel, Branch 1
(Income Tax & Accounting)

cc: