

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **201721007**
Release Date: 5/26/2017
Index Number: 7704.03-00

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:PSI:B03
PLR-130478-14
Date:
February 23, 2017

LEGEND

X =

State =

Date =

Dear :

This letter responds to a letter dated August 7, 2014, submitted on behalf of X by its authorized representative, requesting a ruling under § 7704(d)(1)(E) of the Internal Revenue Code (Code).

FACTS

X is a publicly traded limited partnership organized under State law on Date. X is currently engaged in the transportation, storage, and distribution of refined petroleum products and crude oil. X anticipates engaging in the processing and refining of crude oil condensate through use of a distillation tower (a “splitter”) that will break the crude oil condensate into more valuable refined products (e.g., jet fuel, diesel, gas oil, and light distillates, such as liquefied petroleum gas and naphtha).

X entered into a Tolling Agreement with a single customer to process crude oil condensate in a splitter to be constructed at a bulk petroleum storage terminal that is owned by X. Contemporaneously, X entered into a Connection Agreement and a Revenue Commitment Agreement with the customer to provide bi-directional pipeline transportation services between X’s petroleum terminal and the customer’s petroleum

terminal (the Tolling Agreement, Connection Agreement, and Revenue Commitment Agreement are collectively referred to herein as “the Agreements”).

As part of these Agreements, X committed to construct (or cause to be constructed) certain assets, including the splitter and storage capacity (the facility) and pipelines. X will own, operate, and maintain the facility and pipelines after the assets are placed in service. Under the Tolling Agreement, X will earn (a) a monthly tolling fee based on the volume of condensate processed, and (b) miscellaneous terminalling services fees based upon the volume of product handled and stored. Under the Revenue Commitment Agreement, X will earn a monthly tariff fee based on the volume of the customer’s product that is transported through the pipelines.

The Agreements also provide the customer with the right to terminate the Agreements for any reason and at any time before the date on which the facility and pipelines are placed in service. If the customer exercises such right, the customer would pay X reimbursement payments, an accelerated tolling fee, and an accelerated tariff fee (collectively, the “Termination Income”). The reimbursement payments represent a reimbursement of capital expenditures incurred by X in connection with the partial construction of the facility and pipelines as well as costs that were incurred by X in connection with the customer’s termination of the agreements. Also, X would retain possession and ownership of the construction in process.

X requests a ruling that the Termination Income is qualifying income under § 7704(d)(1)(E).

LAW

Section 7704(a) provides that a publicly traded partnership shall be treated as a corporation. Section 7704(b) provides that the term “publicly traded partnership” means any partnership if (1) interests in that partnership are traded on an established securities market, or (2) interests in that partnership are readily tradable on a secondary market (or the substantial equivalent thereof).

Section 7704(c)(1) provides that § 7704(a) shall not apply to any publicly traded partnership for any taxable year if such partnership met the gross income requirements of § 7704(c)(2) for such taxable year and each preceding taxable year beginning after December 31, 1987, during which the partnership (or any predecessor) was in existence.

Section 7704(c)(2) explains that a partnership meets the gross income requirements of § 7704(c) for any taxable year if 90 percent or more of the gross income of such partnership for such taxable year is qualifying income.

Section 7704(d)(1)(E) provides that the term “qualifying income” includes income and gains derived from the exploration, development, mining or production, processing,

refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resource (including fertilizer, geothermal energy or timber).

Section 1.7704-4(c)(5) of the Income Tax Regulations provides that an activity constitutes processing if it is performed to convert raw mined or harvested products or raw well effluent to substances that can be readily transported or stored, as described in §1.7704-4(c)(5). Section 1.7704-4(c)(5)(ii) provides that an activity constitutes processing of crude oil if it is performed to separate produced fluids by passing crude oil through mechanical separators to remove gas, placing crude oil in settling tanks to recover basic sediment and water, dehydrating crude oil, and operating heater-treaters that separate raw oil well effluent into crude oil, natural gas, and salt water.

Section 1.7704-4(c)(6) provides that an activity constitutes refining if the activity is set forth in §1.7704-4(c)(6). Section 1.7704-4(c)(6)(i)(A) provides that the refining of natural gas and crude oil includes the further physical or chemical conversion or separation processes of products resulting from activities listed in § 1.7704-4(c)(5)(i) and (ii), and the blending of petroleum hydrocarbons, to the extent they give rise to a product listed in § 1.7704-4(c)(5)(i) or (ii) or to the products of a type produced in a petroleum refinery or natural gas processing plant listed in § 1.7704-4(c)(6)(i)(A). Refining of natural gas and crude oil also includes the further physical or chemical conversion or separation processes and blending of the products listed in § 1.7704-4(c)(6)(i)(A), to the extent that the resulting product is also listed in § 1.7704-4(c)(6)(i)(A). Jet fuel, diesel, gas oils, and light distillates, such as liquefied petroleum gas and naphtha, are products listed in § 1.7704-4(c)(6)(i)(A).

Section 1.7704-4(c)(7)(i) provides that an activity constitutes transportation if it is performed to move minerals or natural resources, and products under § 1.7704-4(c)(4), (5), or (6), including by pipeline, marine vessel, rail, or truck. Except as provided in § 1.7704-4(c)(7)(ii), transportation does not include the movement of minerals or natural resources, and products produced under § 1.7704-4(c)(4), (5), or (6), directly to retail customers or to a place that sells or dispenses to retail customers. Retail customers do not include a person who acquires oil or gas for refining or processing, or a utility. Transportation also includes providing storage services.

Section 1.7704-4(c)(10)(i) provides that, if the partnership is in the trade or business of performing a section 7704(d)(1)(E) activity, qualifying income includes income received to reimburse the partnership for its costs in performing that section 7704(d)(1)(E) activity, whether imbedded in the rate the partnership charges or separately itemized. Reimbursable costs may include the cost of designing, constructing, installing, inspecting, maintaining, metering, monitoring, or relocating an asset used in that section 7704(d)(1)(E) activity, or providing office functions necessary to the operation of that section 7704(d)(1)(E) activity (such as staffing, purchasing supplies, billing, accounting, and financial reporting). For example, a pipeline operator that charges a customer for its cost to build, repair, or schedule flow on the pipelines

that it operates will have qualifying income from such activity whether or not it itemizes those costs when it bills the customer.

CONCLUSION

Based solely on the facts submitted and representations made, we conclude that the Termination Income constitutes qualifying income within the meaning of § 7704(d)(1)(E).

Except as specifically provided, we express or imply no opinion as to the federal tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed as to whether X meets the 90 percent gross income requirement of § 7704(c)(1), whether X is a publicly traded partnership within the meaning of § 7704(b), or whether any other type of income not addressed in this ruling is qualifying income under § 7704(d).

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. However, in the event of a technical termination of X under § 708(b)(1)(B), the resulting partnership may continue to rely on this ruling in determining its qualifying income under § 7704(d)(1)(E).

In accordance with the Power of Attorney on file with this office, we are sending copies of this letter to your authorized representatives.

The ruling contained in this letter is 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 ruling request, it is subject to verification on examination.

Sincerely,

/s/

Holly Porter
Chief, Branch 3
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes

cc: