Internal Revenue Service

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In Re:

Department of the Treasury
Washington, DC 20224

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Person To Contact:

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Date:
October 11, 2023

LEGEND:

Taxpayer	=
Corporation	=
Commission	=
State	=
Date 1	=
Date 2	=
Date 3	=
Date 4	=
Commission Docket No. 1	=
Commission Docket No. 2	=
Commission Docket No. 3	=
Commission Docket No. 4	=
A	=
B	=
Month 1	=
Month 2	=
Month 3	=
Year 1	=
Year 2	=

Dear :

A ruling has been requested on behalf of Taxpayer seeking a determination that Taxpayer's reduction in the remaining regulatory life of its public utility property from A years to B years beginning Date 4, is a normalization method of accounting under section 13001(d) of the Tax Cuts and Jobs Act, Pub. L. 115-97, (the "TCJA") and sections 167 and 168 of the Internal Revenue Code of 1986, as amended ("Code"), and regulations thereunder (collectively: “the Normalization Rules”).

FACTUAL BACKGROUND

Taxpayer represents the following facts:

Taxpayer is a regulated public utility incorporated under the laws of State. Taxpayer primarily transports and stores natural gas for utilities, municipalities, gas marketing companies and industrial and commercial users. Taxpayer employs an accrual method of accounting and reports on a calendar year basis. Corporation is incorporated under the laws of State, is a holding company owning subsidiaries engaged in a number of diverse business activities, and is the common parent of a consolidated group of corporations. Corporation employs an accrual method of accounting and reports on a calendar year basis. The consolidated group including Taxpayer and Corporation files a federal consolidated tax return, Form 1120, U.S. Corporation Income Tax Return.

Taxpayer's transportation rates and most of its storage rates, including depreciation costs are determined on a cost-of-service basis and approved by Commission. Depreciation costs are a significant component of Taxpayer's cost of service. Commission requires a composite depreciation rate to be used to depreciate Taxpayer's utility property. To determine appropriate depreciation rates, depreciation studies are performed. These depreciation studies are also used to estimate the remaining average life of the utility assets. Prior to the enactment of the TCJA, the depreciation rates used to determine the average remaining life of the Taxpayer’s associated assets were approved by Commission on Date 1, in Commission Docket No. 1 and Commission Docket No. 2.

Taxpayer depreciates its property using accelerated methods of depreciation under section 168 of the Code for federal income tax purposes. All differences between book and tax depreciation are recorded to the Taxpayer's deferred income tax reserve. Due to limitations in Taxpayer's accounting systems, its books and underlying records do not contain vintage account data**.** Following the enactment of the TCJA, Taxpayer adjusted its deferred income tax reserve as of Date 2 to reflect the reduction in the corporate income tax rate under the TCJA. The excess deferred income tax ("EDIT") balance that resulted was recorded to a regulatory liability that the Taxpayer began to amortize over the remaining average life of the public utility property balances using the Reverse South Georgia Method. The remaining weighted average life used to amortize the EDIT balance was calculated using the depreciation rates approved by Commission on Date 1, weighted by the utility property balances existing on Date 3. Taxpayer began to amortize the EDIT as of Date 2 using a remaining average life of A years.

In Month 1 Year 1, Commission initiated an investigation to determine whether the rates currently charged by Taxpayer were just and reasonable. Taxpayer filed a cost and revenue study with Commission as part of this investigation. In Month 2 Year 1, Taxpayer initiated a rate case, requesting from Commission increases in its transportation and storage rates, including depreciation rates, in Commission Docket No. 3.

In Month 3 Year 2, Commission approved a settlement with Taxpayer, settling both its earlier investigation and the Taxpayer's rate case, including new depreciation rates. The settlement adopted the remaining useful life of relevant assets as concluded in the Taxpayer's study but reduced the number of years remaining in the amortization to reflect that the rates under Taxpayer's rate case for two years prior to the settlement. The settlement, captioned Commission Docket No. 3 and Commission Docket No. 4, provided in relevant part that Taxpayer's regulatory liability attributable to EDIT resulting from the TCJA shall be calculated by using the Reverse South Georgia Method and amortized for a period of B years beginning Date 4.

RULING REQUESTED

Whether the method used by Taxpayer, reducing the remaining regulatory life of its public utility property from A years to B years beginning on Date 4, is considered a normalization method of accounting under section 13001(d) of the TCJA and sections 167 and 168 of the Code.

LEGAL STANDARDS

Normalization Rules in the Code and Regulations

Section 168(f)(2) of the Code provides that the depreciation deduction determined under § 168 of the Code shall not apply to any public utility property (within the meaning of § 168(i)(10) of the Code) if the taxpayer does not use a normalization method of accounting.

In order to use a normalization method of accounting, § 168(i)(9)(A)(i) of the Code requires the taxpayer, in computing its tax expense for establishing its cost of service for ratemaking purposes and reflecting operating results in its regulated books of account, to use a method of depreciation with respect to public utility property that is the same as, and a depreciation period for such property that is not shorter than, the method and period used to compute its depreciation expense for such purposes. Under § 168(i)(9)(A)(ii) of the Code, if the amount allowable as a deduction under § 168 of the Code differs from the amount that would be allowable as a deduction under § 167 of the Code using the method, period, first and last year convention, and salvage value used to compute regulated tax expense under § 168(i)(9)(A)(i) of the Code, the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from such difference.

Section 168(i)(9)(B)(i) of the Code provides that one way the requirements of § 168(i)(9)(A) of the Code will not be satisfied is if the taxpayer, for ratemaking purposes, uses a procedure or adjustment which is inconsistent with such requirements. Under § 168(i)(9)(B)(ii) of the Code, such inconsistent procedures and adjustments include the use of an estimate or projection of the taxpayer's tax expense, depreciation expense, or reserve for deferred taxes under § 168(i)(9)(A)(ii) of the Code, unless such estimate or projection is also used, for ratemaking purposes, with respect to all three of these items and with respect to the rate base.

Former § 167(l) of the Code generally provided that public utilities were entitled to use accelerated methods for depreciation if they used a “normalization method of accounting.” A normalization method of accounting was defined in former § 167(l)(3)(G) of the Code in a manner consistent with that found in § 168(i)(9)(A) of the Code. Section 1.167(l)-1(a)(1) of the Regulations provides that the normalization requirements for public utility property pertain only to the deferral of federal income tax liability resulting from the use of an accelerated method of depreciation for computing the allowance for depreciation under § 167 of the Code and the use of straight-line depreciation for computing tax expense and depreciation expense for purposes of establishing cost of services and for reflecting operating results in regulated books of account. These regulations do not pertain to other book-tax timing differences with respect to state income taxes, F.I.C.A. taxes, construction costs, or any other taxes and items.

Normalization Requirements in the TCJA and Rev. Proc. 88-12

The TCJA, enacted on December 22, 2017, generally reduced the corporate tax rate under § 11 of the Code from 35 percent to 21 percent for taxable years beginning after December 31, 2017. Section 13001(a) of the TCJA.

Section 13001(d) of the TCJA includes accompanying but uncodified normalization requirements related to the reduction of the corporate tax rate.

Section 13001(d)(1) of the TCJA provides that a normalization method of accounting shall not be treated as being used with respect to any public utility property for purposes of §§ 167 or 168 of the Code if the taxpayer, in computing its cost of service for ratemaking purposes and reflecting operating results in its regulated books of account, reduces the excess tax reserve[1] more rapidly or to a greater extent than such reserve would be reduced under the average rate assumption method (“ARAM”).

[1] While the TCJA refers to this excess amount as the excess tax reserve, the commonly used term and the term used throughout this ruling is EDIT.

Rev. Proc. 88-12, 1988-1 C.B. 637, provided similar rules after the Tax Reform Act of 1986 reduced the tax rate from 46 percent to 34 percent. Specifically, Rev. Proc. 88-12 states that:

> [f]or taxable years beginning on or after July 1, 1987, section 601 of the Tax Reform Act of 1986 (Act), 1986-3 (Vol. 1) C.B. 166, reduces from 46 percent to 34 percent the maximum federal income tax applicable to corporations. Section 203(e) of the Act provides rules for reducing the excess tax reserve resulting both from that reduction and from the smaller reduction in rates for tax years starting before and ending after (straddling) July 1, 1987. Section 203(e) of the Act provides that a normalization method of accounting shall not be treated as being used with respect to any public utility property, for purposes of section 167 or 168 of the Internal Revenue Code, f [*sic*] the taxpayer, in computing its cost of service for ratemaking purposes and reflecting operating results in its regulated books of account, reduces its excess tax reserve more rapidly or to a greater extent than such reserve would be reduced under the average rate assumption method.

Sections 3 and 4.01 of Rev. Proc. 88-12 provide that a taxpayer who lacks sufficient vintage account data necessary to apply the ARAM may use the "Reverse South Georgia Method." In general, a taxpayer uses the Reverse South Georgia Method if it: (a) computes the excess tax reserve on all public utility property included in the plant account on the basis of the weighted average life or composite rate used to compute depreciation for regulatory purposes, and (b) reduces the excess tax reserve ratably over the remaining regulatory life of the property.

Section 13001(d)(2) of the TCJA provides that certain taxpayers may use an alternative method, and in relevant part states that if the taxpayer was required by a regulatory agency to compute depreciation for public utility property on the basis of an average life or composite rate method, and the taxpayer's books and underlying records did not contain the vintage account data necessary to apply the average rate assumption method, the taxpayer will be treated as using a normalization method of accounting if, with respect to such jurisdiction, the taxpayer uses the alternative method for public utility property that is subject to the regulatory authority of that jurisdiction.

Section 13001(d)(3)(A) of the TCJA defines the term “excess tax reserve” to mean the excess of (i) the reserve for deferred taxes (as described in § 168(i)(9)(A)(ii) of the Code as of the day before the corporate rate reductions provided in the amendments made by this section take effect, over (ii) the amount which would be the balance in such reserve if the amount of such reserve were determined by assuming that the corporate rate reductions provided in this Act were in effect for all prior periods.

Section 13001(d)(3)(B) of the TCJA defined ARAM and provides that the ARAM is the method under which the excess in the reserve for deferred taxes is reduced over the remaining lives of the property as used in its regulated books of account which gave rise to the reserve for deferred taxes. Under such method, during the time period in which the timing differences for the property reverse, the amount of the adjustment to the reserve for the deferred taxes is calculated by multiplying (i) the ratio of the aggregate deferred taxes for the property to the aggregate timing differences for the property as of the beginning of the period in question, by (ii) the amount of the timing differences which reverse during such period.

Section 13001(d)(3)(C) of the TCJA defines "alternative method" as the method in which the taxpayer: (i) computes the excess tax reserve on all public utility property included in the plant account on the basis of the weighted average life or composite rate used to compute depreciation for regulatory purposes, and (ii) reduces the excess tax reserve ratably over the remaining regulatory life of the property.

ANALYSIS

The TCJA provided normalization requirements for the EDIT with respect to public utility property. These requirements limit how regulated public utilities and their regulators reduce the amount of EDIT associated with restating accumulated deferred income taxes ("ADIT") arising from method and life depreciation differences for public utility property. The normalization language in the TCJA limits the amount by which the owner of public utility property is permitted to reduce EDIT to ARAM or, if the requirements are satisfied, the alternative method.

Here, Taxpayer's books and underlying records do not contain the vintage account data necessary to apply ARAM, and as a result, under section 13001(d)(2) of the TCJA, Taxpayer is permitted to use the alternative method for public utility property that is subject to the regulatory authority of that jurisdiction. Taxpayer has used the Reverse South Georgia Method to reduce its EDIT ratably over the weighted average remaining regulatory life of the related assets. This method was approved by Commission on Month 3 Year 2, in Commission Docket No. 3 and Commission Docket No. 4, in a settlement providing that Taxpayer's regulatory liability attributable to EDIT resulting from TCJA will be amortized using the Reverse South Georgia Method over a period of B years as of Date 4. Because the Reverse South Georgia Method constitutes an alternative method as permitted by section 13001(d)(2) of the TCJA, Taxpayer's reduction in the remaining regulatory life of its public utility property from A years to B years beginning Date 4, is a normalization method of accounting.

CONCLUSION

Based on the foregoing, we conclude that Taxpayer's reduction in the remaining regulatory life of its public utility property from A years to B years beginning Date 4, is a normalization method of accounting under section 13001(d) of the TCJA and sections 167 and 168 of the Code.

Except as specifically set forth above, no opinion is expressed or implied concerning the federal income tax consequences of the above-described facts under any other provision of the Code or regulations.

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.

This ruling is based upon information and representations submitted by Taxpayer and accompanied by penalty of perjury statements 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.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

Sincerely

Patrick S. Kirwan
Chief, Branch 6
Office of the Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosure:
Copy for § 6110 purposes

cc: