

LAW AND ANALYSIS

Section 61(a) and section 1.61-1 of the Income Tax Regulations provide that gross income means all income from whatever source derived, unless excluded by law. Section 118(a) provides that, in the case of a corporation, gross income does not include any contribution to the capital of the taxpayer. Section 118(b), as amended by section 824(a) of the Tax Reform Act of 1986 (the Act), provides that for section 118(a) purposes, the term “contribution to the capital of the taxpayer” does not include any contribution in aid of construction (CIAC) or any other contribution as a customer or potential customer.

Before the Act, former section 118(b) allowed certain regulated public utilities to exclude from gross income as contributions to the capital of the corporation certain contributions made by a customer or potential customer in aid of construction. Section 824(a) of the Act repealed this special exclusion by amending section 118(b). The changes made by the Act apply to all contributions after that date. As a result of this change, all CIACs, even those received by a regulated public utility such as Corp A, are includible in gross income. Although not applicable to Corp A, section 118 was subsequently amended by the Small Business Job Protection Act of 1996 to restore the benefits of the provisions repealed by the Act for regulated public utilities that provide water or sewage disposal service.

The House Ways and Means Committee Report for the Act explains that property, including money, is a CIAC (rather than a capital contribution) if it is transferred to provide or encourage the provision of services to or for the benefit of the person transferring the property. H.R. Rep. No. 426, 99th Cong., 1st Sess. 644 (1985), 1986-3 (Vol. 2) C.B. 644 (the House Report). A utility has received property to encourage the provision of services if the receipt of the property is a prerequisite to the provision of the services; if the receipt of the property results in the provision of services earlier than would have been the case had the property not been received; or if the receipt of the property otherwise causes the transferor to be favored in any way. Id. The House Report also states that the repeal of the special exclusion does not affect transfers of property that are not made in connection with the provision of services, including situations where it is clearly shown that the benefit of the public as a whole was the primary motivating factor in the transfers. Id.

Notice 87-82, 1987-2 C.B. 389, provides additional guidance. Notice 87-82 follows the language from the House Report and states that a payment received by a utility is not a CIAC if it does not reasonably relate to the provision of services by the utility to or for the benefit of the person making the payment, but rather relates to the benefit of the public at large. Notice 87-82 provides as an example of a payment benefiting the public at large a relocation payment received by a utility under a government program to place utility lines underground. In that situation, the relocation payment is not considered a CIAC where the relocation is undertaken for purposes of community aesthetics and public safety and does not directly benefit particular

customers of the utility in their capacity as customers. Notice 87-82 provides as an additional example reimbursements received by a utility for the costs of relocating utility lines to accommodate the construction or expansion of a highway and not for the provision of utility services.

Notice 87-82 states that in other cases, however, relocation fees are treated as CIACs and included in gross income because they relate to the provision of services by the utility to or for the benefit of the person making the payment. For example, assume that a potential customer of a utility is required (either by the utility or by a governmental entity) to pay the utility for the costs of relocating utility facilities in order to obtain access to utility services for a site the customer is developing. Since the payment of the relocation fees is a prerequisite to obtaining utility services, the payment is a CIAC and is included in the utility's income, regardless of whether the particular utility facilities being relocated are related to the site the customer is developing.

Under the site approval plan, Developer could not develop the site without relocating the utility poles and lines and connecting to the relocated utility poles and lines. Consequently, the payments made by Developer to Corp A to relocate the utility poles and lines and to connect to the relocated utility poles and lines are a CIAC because they relate to the provision of services by Corp A for the benefit of Developer.

CONCLUSION

Accordingly, based solely on the foregoing analysis and the representations made, we conclude that the payments made by Developer to Corp A to relocate the utility poles and lines and to connect to the relocated utility poles and lines are a CIAC under section 118(b) included in gross income under section 61.

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 who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter should be filed with Parent's federal income tax return for the taxable year in which the payment is made.

In accordance with the power of attorney on file with this ruling request, a copy of this letter is being sent to Parent's authorized representative.

Sincerely,

SUSAN J. REAMAN
Branch Chief, Branch 5
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2):

Copy of this letter

Copy for section 6110