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In Re:

Date:
May 30, 2019

LEGEND

Taxpayer =
Subsidiary 1 =
Subsidiary 2 =
Location 1 =
Location 2 =
Date 1 =
Date 2 =
Date 3 =
Date 4 =
Date 5 =
Date 6 =
Date 7 =
Year =
a =
b =
c =

Dear :

This letter responds to a request for a ruling dated January 22, 2019, submitted by Taxpayer on behalf of Subsidiary 1 and Subsidiary 2, concerning the application of sections 48 and 481 of the Internal Revenue Code (the "Code") to the facts described below.

The relevant facts as represented in Taxpayer's submission are set forth below.

Subsidiary 1 and Subsidiary 2 (collectively referred to as "the Subsidiaries") are subsidiary corporations wholly owned by Taxpayer. Taxpayer is the common parent of an affiliated group of corporations including the Subsidiaries that file a consolidated federal income tax return on an accrual method of accounting with a tax year ending on Date 1. Taxpayer's consolidated group provides energy and natural gas services including transportation, distribution, and asset management across the Location 1 and Location 2. The Subsidiaries invest in, own, and operate solar and onshore wind projects with a total capacity of nearly a megawatts that provide residential and commercial customers with low-carbon emission solutions to generate clean power.

For each of the fiscal taxable years ending Date 2 through Date 6, Subsidiary 1 placed in service self-constructed property that uses solar energy to generate electricity. Similarly, for each of the fiscal taxable years ending Date 3 through Date 6, Subsidiary 2 placed in service self-constructed property which uses solar energy to generate electricity. Taxpayer determined that this self-constructed property satisfied the definition of qualified energy property as defined under § 48(a)(3) and claimed a 30 percent § 48 credit on the cost basis of such property placed in service in each applicable fiscal taxable year.

On Date 7, Taxpayer filed a Form 3115, Application for Change in Accounting Method, under the automatic consent procedures provided in Revenue Procedure 2017-30. Pursuant to this automatic accounting method change, Taxpayer computed a net positive § 481(a) adjustment equal to b to reflect the difference as of Date 5 (the beginning of the year of change) between the adjusted basis of the self-constructed property under Taxpayer's present and proposed methods. Taxpayer represents that the § 481(a) adjustment includes the amount of mixed service costs capitalizable, as determined under the direct reallocation method described in Treas. Reg. § 1.263A-1(g)(4)(iii)(A), to Taxpayer's self-constructed property that was placed in service during fiscal tax years ending Date 2 through Date 4, less the amount of allowable depreciation as of the beginning of the year of change.

As represented by Taxpayer the net positive § 481(a) adjustment attributable to costs not originally capitalized to the self-constructed property net of the allowable accumulated depreciation pursuant to the new method of accounting is c. This amount is attributable to self-constructed property placed in service by both of the Subsidiaries.

RULING REQUESTED

Taxpayer may claim additional investment tax credits under § 48 on its amended federal income tax return for the taxable year ended Date 6 (i.e., the year of change) on the increased amount of the depreciable cost basis determined pursuant to its accounting method change, on the basis that fiscal Year was the first taxable year after the energy property was placed in service that the additional capitalized costs were property reflected in the depreciable cost basis of the energy property.

LAW AND ANALYSIS

Section 38(b)(1) authorizes taxpayers to claim a current year business credit which is the sum of several credits, including the investment credit determined under § 46. In turn, the § 46 investment credit is the sum of several credits, including the energy credit under § 48.

Section 48(a)(1) generally provides that, for purposes of § 46, the energy credit for any taxable year is the energy percentage of the basis of each energy property placed in service during such taxable year. Section 48(a)(3)(A)(i) provides that energy property includes equipment that uses solar energy to generate electricity, to heat or cool (or provide hot water for use in) a structure, or to provide solar process heat, excepting property used to generate energy for the purposes of heating a swimming pool. Section 48(a)(2)(A)(i) provides that the energy percentage for solar energy property is 30 percent. This energy percentage is subject to a phase out based on the year in which construction of the solar energy property begins as provided in § 48(a)(6).

While § 48 and the Treasury Regulations promulgated thereunder define the property to which the investment credit is applicable and the percentage of the qualifying basis, the Treasury Regulations promulgated under § 46 provide the rules to calculate the qualified investment subject to the credit. Under Treas. Reg. § 1.46-3(a), the qualified investment of the taxpayer, with respect to any taxable year, is generally the aggregate of: (1) the applicable percentage of the basis of each new § 38 property placed in service by the taxpayer during the taxable year; plus (2) the applicable percentage of the cost of each used § 38 property placed in service by the taxpayer during such taxable year.

Treasury Regulation § 1.46-3(c) states generally that the basis of any new § 38 property shall be determined in accordance with the general rules for determining the basis of property. Thus, the basis of property would generally be its cost determined under the provisions of § 1012.

Treasury Regulation § 1.46-3(d)(1) explains that for purposes of the investment credit, property is considered placed in service in the earlier of following taxable years: (i) the taxable year in which, under the taxpayer’s depreciation practice, the period for depreciation with respect to such property begins; or (ii) the taxable year in which the property is placed in a condition or state of readiness and availability for a specifically assigned function.

Treasury Regulation § 1.46-3(d)(4)(i) explains, in part, that the investment credit allowed by § 38 with respect to any property shall be allowed only for the first taxable year in which such property is placed in service by the taxpayer. The determination of

whether property is § 38 property in the hands of the taxpayer shall be made with respect to such first taxable year.

Treasury Regulation § 1.46-3(d)(4)(ii) explains that notwithstanding subdivision (i) of this subparagraph, if, for the first taxable year in which property is placed in service by the taxpayer, the property qualifies as § 38 property but the basis of the property does not reflect its full cost for the reason that the total amount to be paid or incurred by the taxpayer for the property is indeterminate, a credit shall be allowed to the taxpayer for such first taxable year with respect to so much of the cost as is reflected in the basis of the property as of the close of such year, and an additional credit shall be allowed to the taxpayer for any subsequent taxable year with respect to the additional cost paid or incurred during such year and reflected in the basis of the property as of the close of such year.

Section 50(c)(1) provides that if a credit is determined under this subpart with respect to any property, the basis of such property shall be reduced by the amount of the credit so determined. Section 50(c)(2) provides that if during any taxable year there is a recapture amount determined with respect to any property, the basis of which was reduced under § 50(c)(1), the basis of such property (immediately before the event resulting in recapture) shall be increased by an amount equal to such recapture amount. For these purposes, the term "recapture amount" means any increase in tax "or adjustment in carrybacks or carryovers) determined under § 50(a)." Additionally, § 50(c)(3) provides that in the case of the energy credit, only 50 percent of such credit shall be taken into account under § 50(c)(1) and only 50 percent of any recapture amount attributable to such credit shall be taken into account under § 50(c)(2).

Treasury Regulation § 1.48-1(b)(1) provides, in relevant part, that property is not § 38 property unless a deduction for depreciation (or amortization in lieu of depreciation) with respect to such property is allowable to the taxpayer for the taxable year. A deduction for depreciation is allowable if the property is of a character subject to the allowance for depreciation under § 167 and the basis (or cost) of the property is recovered through a method of depreciation.

Treas. Reg. § 1.48-1(b)(3) provides, in relevant part, that if the cost of property is not recovered through a method of depreciation but through a deduction of the full cost in one taxable year, for purposes of § 1.48-1(b)(1), a deduction for depreciation with respect to such property is not allowable to the taxpayer. However, if an adjustment with respect to the income tax return for such taxable year requires the cost of such property to be recovered through a method of depreciation, a deduction for depreciation will be considered allowable to the taxpayer.

Section 481 prescribes the rules to be followed in computing taxable income in cases where the taxable income of the taxpayer is computed under a method of accounting different from that under which the taxable income was previously

computed. Section 481(a)(2) provides that the taxpayer shall take into account the adjustments necessary solely by reason of the change to prevent amounts from being duplicated or omitted, and the adjustments resulting from a change in accounting method will include only those amounts that are determined to be necessary solely by reason of the change, and there shall not be taken into account any adjustment in respect of any taxable year other than the year of change, unless the change was initiated by the taxpayer.

Treas. Reg. § 1.481-1(a)(1) provides, in relevant part, that in computing taxable income for the taxable year of the change, there shall be taken into account those adjustments that are determined to be necessary solely by reason of such change in order to prevent amounts from being duplicated or omitted. The year of change is the taxable year for which the taxable income of the taxpayer is computed under a method of accounting different from that used for the preceding taxable year.

CONCLUSION

Taxpayer represents that its new accounting method capitalizes more costs to the self-constructed property than Taxpayer's previous method. The § 481(a) adjustment increases the basis of the property to prevent the taxpayer from being unable to recover costs that were not capitalized under the previous method, but are capitalized under the new method (a duplication of income). Once the method change has been implemented and the § 481(a) adjustment taken into account, Taxpayer has a higher basis in the property, reflecting the additional capitalizable costs, just as though Taxpayer had been using the new method of accounting all along.

As a result, Taxpayer may claim additional investment tax credits under § 48 on its amended federal income tax return for the taxable year ended Date 6 (i.e., the year of change) on the increased amount of the depreciable cost basis determined pursuant to its accounting method change, on the basis that fiscal Year was the first taxable year after the energy property was placed in service that the additional capitalized costs were property reflected in the depreciable cost basis of the energy property.

Except as specifically determined above, no opinion is expressed or implied concerning the Federal income tax consequences of the facts described above under any other provision of the Code. Specifically, no opinion is expressed or implied as to whether Taxpayer's change of accounting method was properly made, the propriety or application of Taxpayer's methods of capitalizing all costs required to be capitalized under § 263A and the implementing regulations, or whether the amount of the § 481(a) adjustment, including the amount giving rise to the § 48 credit, was correctly determined. Additionally, no opinion is expressed or implied as to whether Taxpayer properly calculated and claimed the § 48 credit on the solar energy property.

The ruling contained in this letter is based upon information and representations submitted by 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 upon examination.

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. In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representatives. We are also sending a copy of this letter to the appropriate Director (LB&I).

A copy of this ruling must be attached to any federal 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.

Sincerely,

Peter C. Friedman
Senior Technician Reviewer, Branch 6
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

cc: