

Internal Revenue Service

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Date:
September 17, 2021

LEGEND:

Parent =

Corporation =

Taxpayer =

State =

Commission =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Year 1 =

a =

b =

c =

d =

Docket 1 =

Docket 2 =

Dear :

This letter responds to a request for a private letter ruling dated March 12, 2021, and additional submission dated August 23, 2021, submitted on behalf of Taxpayer. Taxpayer requests a ruling on the application of section 13001(d) of Public Law 115-97 (commonly known as the “Tax Cuts and Jobs Act” or “TCJA”) specifically as well as generally the application of § 168(i)(9) of the Internal Revenue Code, former § 167(l), and § 1.167(l)-1 of the Income Tax Regulations (collectively referred to as the Normalization Rules). The relevant facts as represented in Taxpayer’s submission are set forth below.

FACTS

Parent is a corporation organized under the laws of State. Parent’s fiscal year for accounting purposes is the calendar year, and it uses the accrual method of accounting in maintaining its books and for tax purposes. Parent is the common parent of a consolidated group of corporations that includes Corporation, a corporation organized under the laws of State. Corporation’s fiscal year for accounting purposes is the calendar year, and it uses the accrual method of accounting in maintaining its books and for tax purposes. Corporation owns indirectly all of the partnership interests in Taxpayer, a State limited partnership which is disregarded as an entity separate from Corporation for federal income tax purposes.

Parent provides natural gas and liquids transportation services in interstate and intrastate commerce throughout the United States, connecting major supply basins to existing and growing energy markets. Corporation owns and operates a portfolio of natural gas-related energy assets in North America that provide transmission, storage, gathering, distribution, and processing services. Taxpayer is a regulated natural gas company under the Natural Gas Act that engages in the interstate transportation of natural gas through its pipeline system extending through several states. Taxpayer is a “public utility” for purposes of the TCJA.

Taxpayer’s rates for providing interstate natural gas transmission services (jurisdictional services) are subject to the Commission. As part of setting rates and pursuant to Section 9 of the Natural Gas Act, Commission establishes the rates of depreciation applicable to the property used by a Commission-regulated natural gas company to provide jurisdictional services (jurisdictional property). For ratemaking

purposes and for purposes of reflecting operating results on its books, Taxpayer uses a single composite depreciation rate. The depreciation rate and Taxpayer's jurisdictional property existing on the day rates go into effect are used to calculate the average remaining life of Taxpayer's assets for ratemaking purposes. On Date 1, Taxpayer's Commission-approved onshore transmission depreciation rate, which constitutes the depreciation rate for the vast majority of Taxpayer's pipeline system, was a%. This depreciation rate was approved by Commission in Year 1 in Docket 1. The application of this rate to Taxpayer's jurisdictional property resulted in an average remaining life for its jurisdictional property of b years.

For federal income tax purposes, Taxpayer depreciates its property using accelerated methods of depreciation under § 168 of the Internal Revenue Code of 1986. As required by § 168(i)(9), Taxpayer uses a normalization method of accounting for regulatory purposes. Accordingly, in computing its tax expense for ratemaking purposes and for reflecting operating results on its regulated books of account, Taxpayer uses a depreciation method and period that is consistent with the depreciation used for ratemaking purposes. Adjustments are made to a deferred tax reserve (generally referred to as the "Accumulated Deferred Income Taxes" or "ADIT") to account for the difference between its actual tax expense and its tax expense as computed for ratemaking purposes. ADIT reflects all differences between book depreciation and tax depreciation including, but not limited to, accelerated depreciation. Taxpayer's ADIT became overfunded as of Date 2 due to the reduction in corporate tax rates affected by the TCJA. The portion of the excess amount in ADIT attributable to accelerated depreciation is referred to herein as the "Protected EDIT". The amount of the Protected EDIT is calculated based on Taxpayer's jurisdictional property existing at the time the Protected EDIT is established.

Ratemaking Proceeding and Settlement Agreement

On Date 3, Taxpayer filed revised tariff records with Commission proposing changed rates in Docket 2. On Date 4, Taxpayer and the parties to the Docket 2 proceeding filed a Stipulation and Agreement memorializing a settlement in principle (the "Settlement"). The Settlement provides for new tariff rates that became effective retroactively as of Date 5. Upon approval of the Settlement, Taxpayer's depreciation rate for ratemaking purposes for its onshore transmission system increased from a% to c%. The change to the depreciation rate was calculated using an analysis of depreciation and salvage rates for such jurisdictional property. The application of the Settlement depreciation rates to Taxpayer's jurisdictional property as of Date 5 results in an average remaining life for that property of d years as of that date.

In the Settlement, the parties agreed that Taxpayer would seek a private letter ruling from the Internal Revenue Service (the "IRS") requesting the IRS to rule that amortizing the Protected EDIT over d years – the remaining regulatory life of Taxpayer's jurisdictional property as of the effective date of the new rates (i.e. Date 5) – would not result in a normalization violation. The parties further agreed that Taxpayer will

amortize the Protected EDIT over d years if the IRS rules that using d years would not result in a normalization violation. If the IRS determines that using the d year amortization would result in a normalization violation, Taxpayer will continue to amortize the Protected EDIT over b years.

The Stipulation and Agreement remains in effect as of the date of the PLR submission.

RULING REQUESTED

Taxpayer requests a ruling that Taxpayer would not violate the normalization requirement set forth in section 13001(d) of the TCJA if it began amortizing the Protected EDIT ratably over d years beginning on Date 5.

LAW AND ANALYSIS

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

In order to use a normalization method of accounting, § 168(i)(9)(A) requires that a 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, 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), if the amount allowable as a deduction under § 168 differs from the amount that would be allowable as a deduction under § 167 using the method, period, first and last year convention, and salvage value used to compute regulated tax expense under § 168(i)(9)(A)(i), the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from such difference.

Former section 167(l) 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) in a manner consistent with that found in § 168(i)(9)(A). Section 1.167(l)-1(a)(1) 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 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.

In addition to the normalization requirements set forth in section 168(i)(9), 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) 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] 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 more rapidly or to a greater extent than such reserve would be reduced under the average rate assumption method” (ARAM).

Section 13001(d)(2) of the TCJA provides an alternative method for certain taxpayers. If, as of the first day of the taxable year that includes the date of enactment of the TCJA, 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 ARAM, 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 “excess tax reserve” as the excess of (i) the reserve for deferred taxes as described in § 168(i)(9)(A)(ii) as of the day before the corporate rate reductions made by the TCJA 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 the TCJA were in effect for all prior periods.

Section 13001(d)(3)(B) of the TCJA provides, in part, that under ARAM, 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.

Section 13001(d)(3)(C) of the TCJA defines the alternative method as the method in which the taxpayer 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 reduces the excess tax reserve ratably over the remaining regulatory life of the property. The alternative method is also known as the Reverse South Georgia Method (“RSGM”).

Commission continues to allow entities subject to its jurisdiction to amortize the Protected EDIT using either ARAM or the RSGM, which is permitted as an exception, if a rate regulated company does not have vintage records for its plant assets to support the reversal of book/tax differences. Commission requires Taxpayer to depreciate its jurisdictional property using a composite depreciation rate, and Taxpayer's books and records lack the vintage account data necessary to use ARAM. Thus, Taxpayer may

amortize its Protected EDIT using the alternative method described in section 13001(d)(3)(C) of the TCJA. Taxpayer will be using the RSGM, the alternative method adopted by Commission, to amortize the Protected EDIT.

Under section 13001(d)(3)(C) of the TCJA, Taxpayer's Protected EDIT must be amortized "over the remaining regulatory life of the property." Section 13001(d)(3)(C) of the TCJA does not specifically state whether the regulatory authority (that is, Commission in this case) must determine the "remaining regulatory life of the property" as of any specific date. The Settlement is the first time Taxpayer's Commission-approved depreciation rates changed since passage of the TCJA.

Taxpayer's use of an average remaining life of Taxpayer's jurisdictional property calculated using the Commission-approved composite depreciation rate that changed after passage of the TCJA and was approved in the Settlement does not violate the Normalization Rules per se. That is, amortizing Protected Edit using a revised depreciation rate and thus average remaining life is not prohibited by the Normalization Rules. However, § 1.167(l)-1(a)(1) 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 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. Here, the change to the depreciation rate was based on an analysis of the depreciation and salvage rates of Taxpayer's existing jurisdictional property. Such factors are within § 1.167(l)-1(a)(1) and therefore the revised depreciation rate adopted in the Settlement Agreement and the resulting change in the average remaining life for that property do not violate the Normalization Rules.

We note that cost of removal (COR) amounts are not protected by the Normalization Rules. While COR may be a component of the calculation of the amount treated as book depreciation, it is a deduction under § 162 and has nothing to do with actual accelerated tax depreciation. While depreciation method and life differences are created and reversed solely through depreciation, such is not the case with COR. While the COR timing differences may often originate as a component of book depreciation, it reverses through the incurred COR expenditure. If factors such as COR were used to revise the depreciation rate, such use could result in an impermissible acceleration of the return of the deferred taxes to ratepayers in violation of the Normalization Rules.

Based on the foregoing, we conclude that Taxpayer would not violate the normalization requirement set forth in section 13001(d) of the TCJA if it began amortizing the Protected EDIT ratably over years beginning on Date 5.

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,

/s/

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

Enclosure:
Copy for § 6110 purposes

cc: