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# Energy Law ALERT

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## Facility-Specific Power Purchase Agreements Are Part of the Facility

The Internal Revenue Service recently ruled that certain facility-specific power purchase agreements (PPAs) are considered part of the underlying energy facility, and are not separate property. In PLR 201214007, an electric company acquired all of the membership interests in an unrelated entity that owned and operated (or was constructing) wind energy facilities. The entity had entered into PPAs that obligated the energy producer to sell and, the purchaser to buy, all or a specified cap amount of electricity that was produced at that specific facility at a specified price for a specified term of years. In the case of a specified cap amount, some PPAs contained a price adjustment for sales in excess of the cap amount. Under no circumstances could the entity fulfill its obligations under the PPAs from sources other than the specified energy facility. As a result, a transfer of a PPA without a transfer of the related wind energy facility would leave the transferee with no way to satisfy the PPA.

The PPAs had significant value because energy rates had fallen since the PPAs' execution. The taxpayer did not want to allocate any of the purchase price to the PPAs, which would have had to be amortized over 15 years, rather than the five year depreciation period for the energy facilities. The IRS agreed. Because each PPA could only be satisfied with the power produced at the specified facility designated in the PPA, the IRS determined that the facility-specific PPA was not a separate asset from the wind energy facility. Although the ruling is based on wind energy facilities, the analysis should apply to other types of energy property. Private letter rulings may only be relied on by the requesting taxpayer and may not be used or cited as precedent, but generally indicate the IRS's position on particular issues.

The ruling may also support a position that the PPA should be taken into account in determining Treasury Section 1603 cash grants (which expired December 31, 2011, subject to commencement of construction by that date) and investment tax credits. The major benefit would come from grants and credits which are based on value, and not just cost. With respect to cash grants, the Treasury had previously implied that PPAs with significant value are generally separate non-qualified property. Whether the Treasury will modify its position in light of the IRS ruling is not clear.

If you have any questions, please contact Alan J. Tarr at atarr@loeb.com or 212.407.4900.

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