

Contributions in Aid of Construction

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Background – Code § 118(a)

- Code § 118(a): In the case of a corporation, gross income does not include any contribution to the capital of a corporation.
- Treas. Reg. § 1.118-1: The exclusion does not apply to any money or property transferred to the corporation in consideration for goods or services rendered.
- 1954 Legislative History: Code incorporated judicial decisions (Brown Shoe). Contributor may expect to derive indirect benefits, but the anticipated future benefits may be so intangible as to not warrant treating the contribution as a payment for future services.

- Code § 118(b): Contribution to the capital of a taxpayer (“TP”) does not include any contribution in aid of construction (“CIAC”) or any other contribution as a customer or potential customer.
- 1986 Legislative History: A utility is considered as having 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. However, contributions motivated primarily for the benefit of the public as a whole are not CIACs and remain excludible.

Background – Notice 87-82

- Tax treatment of many relocation fees not affected by 1986 amendment to Code § 118(b). Examples given include payments for moving utility lines for highway construction or expansion and for undergrounding utility lines.
- Consider whether contribution relates to the provision of services by TP or benefits contributor versus whether it relates to the benefit of public at large.
- Contribution is included in income even where contributor is governmental entity or where facility receiving services operates for benefit of public at large.

- Key factors include:
 - Is contributor a current or future customer of TP?
 - Will residents of contributor's project become future customers of TP?
 - Will relocated or new facilities provide additional or upgraded services to contributor in future?
 - Will relocated or new facilities tie into existing facilities that will serve contributor or future residents of contributor's project?

- Additional key factors include:
 - What is benefit to public at large?
 - What is purpose of facility prompting relocation or contribution?
 - Is source of contribution bonds or a public fund?
 - Is contributor a public entity?
 - Can contributor's project proceed without contribution?
 - Is project merely an undergrounding?

Trends in PLRs

- Only twelve rulings since 1/1/2005.
- More favorable rulings were issued in earlier years.
- Had been a period of time where IRS seemed to rule favorably only on undergrounding scenarios. IRS asserted that it did not agree with earlier rulings, but did not withdraw them. IRS seemed to require that public benefit be “sole” motivation as opposed to “primary” motivation for contribution.
- Recently IRS seems more open-minded in consideration of rulings under Code § 118, although IRS denies any change in policy.

- TP would receive payments from a county program to relocate a transmission line to accommodate a public road project.
- Transmission line serves current and proposed electrical substations for existing and proposed developments in the area but will not serve any part of development prompting roadway realignment.
- At a future date, developer prompting the road expansion, in cooperation with TP, will install 12kV and lower lines to serve its project, but these lines will not tie into the relocated transmission line.

- County program designed to identify and fund road system improvements for new developments within the County and is funded by local developers and state and federal revenues.
- IRS stated that the payments to TP to relocate the transmission line will benefit the public at large by widening a public highway and therefore concluded that they fall within the public benefit exception in Notice 87-82 so are not taxable CIACs under Code § 118(b).
- IRS stated that the payments also contain the characteristics of a nonshareholder contribution to capital described in Chicago Burlington and therefore concluded that they are a non-taxable contribution to the capital of TP under Code § 118(a).

- Trend is looking up.
- Law supports continued favorable outcomes.
- Appears to have taken hold at IRS National Office.
- TPs should consider offering contributors option of bearing costs and risks of seeking private guidance in lieu of CIAC gross up.