

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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LEGEND

Partner =

Parent =

LLC =

ProjectCo =

Trust =

Agency =

State A =

State B =

County =

a =

c =

d =

e =

State C =

f =

g =

h =

Dear

This letter responds to your letter dated December 10, 2003, requesting rulings on behalf of Projectco, regarding ProjectCo's qualification for tax credits under section 45 of the internal Revenue Code.

You represent that the facts are as follows.

Partner is an entity that is disregarded as an entity separate from its owner for federal income tax purposes. All of the membership interests in Partner are owned by LLC, a State A limited liability company. LLC is a direct wholly-owned subsidiary of Parent, a State C corporation. ProjectCo is a State A limited liability company, which was formed on a, for the purpose of developing and owning the Project. ProjectCo is owned by Partner and an affiliated corporation. ProjectCo is treated as a partnership for federal income tax purposes. The Project is an e megawatt wind-based generation project consisting of e separate MW wind turbine generators located in County.

The Trust is a tax-exempt organization formed in response to State B legislation to establish a g percent public purposes charge to the rates paid by the customers of f utilities in State B for, among other things, the above-market costs of renewable energy resources. State B laws authorize Agency to direct the manner in which the funds are collected and spent. State B laws further provide Agency with the authority to direct that funds collected be paid to a nongovernmental entity for investment in, among other things, renewable energy resources. The Trust is this nongovernmental entity.

ProjectCo has agreed to transfer the environmental attributes (including all credits, benefits, emissions, reductions, offsets, and allowances resulting from the avoidance of any emission of any gas, chemical, or other sources) associated with the production of electricity at the project to Trust in exchange for an advance payment (the "Advance Payment"). ProjectCo will earn the Advance Payment as it delivers kilowatt hours of electricity to the utility that has agreed to buy power from the Project. ProjectCo must repay Trust an amount equal to any portion of the Advance Payment that has not been earned by the 15<sup>th</sup> year after commencement of commercial operations.

State B provides a transferable, nonrefundable business energy tax credit (the "BETC") in the amount of c percent of up to \$d million of the cost of energy or conservation projects, including wind projects, for projects located in Sate B. The BETC may be used to offset State B income tax over an h-year period. ProjectCo expects the project to qualify for the BETC. ProjectCo expects to transfer the right to the BETC to LLC who will then sell the BETC to an unrelated entity for an amount approximately the present value of the BETC.

Partner requests the following ruling on behalf of ProjectCo:

The Advance Payment and the BETC will not be considered 1) a grant provided by the United States, a state, or a political subdivision of a state for use in connection with the Project; 2) proceeds of an issue of state or local government obligations used to provide financing for the Project the interest on which is exempt from tax under § 103; 3) subsidized energy financing provided (directly or indirectly) under a federal, state, or local program provided in connection with the Project; or 4) an other credit within the meaning of § 45(b)(3)(A)(iv).

Under § 45, the renewable electricity production credit for any taxable year is an amount equal to the product of 1.5 cents, multiplied by the kilowatt hours of electricity 1) produced by the taxpayer from qualified energy resources, and at a qualified facility during the 10-year period beginning on the date the facility was originally placed in service, and 2) sold by the taxpayer to an unrelated person during the taxable year.

Under § 45(b)(3), the amount of the credit with respect to any project for any taxable year is reduced by an amount equal to the product of 1) the amount of the credit otherwise allowable for such year and 2) a fraction, the numerator of which is the sum of i) grants provided by the United States, a State, or a political subdivision of a State for use in connection with the project; ii) proceeds of an issue of State or local government obligations used to provide financing for the project the interest on which is exempt from tax under § 103; iii) the aggregate amount of subsidized energy financing provided (directly or indirectly) under a Federal, State of local program in connection with the project; and iv) the amount of any other credit allowable with respect to any property which is part of the project, and the denominator of which is the aggregate amount of additions to the capital account for the project for the taxable year and all prior taxable years.

A similar reduction exists under § 29(b)(3) relating to governmental grants or subsidized energy financing provided in connection with a nonconventional source fuel project. Section 29 was added to the Code as a part of the Crude Oil Windfall Profit Tax of 1980, section 231, 1980-3 C.B. 1, 40. The Conference Report, in explaining the reduction mechanism found in § 29(b)(3), states that the § 29 credit is reduced in proportion to federal grants provided in connection with the construction or acquisition of the facility. H.R. Rep. No. 96-817 (Conf. Rep.), 96<sup>th</sup> Cong., 2d Sess. (1980), 1980-3 C.B. 245, 300.

Section 45(c)(1) defines “qualified energy resources” to include wind. Section 45(c)(3)(A) defines a “qualified facility” in the case of a facility using wind to produce electricity as any facility owned by the taxpayer that is originally placed in service after December 31, 1993, and before January 1, 2004.

Section 45 does not define the term “grant.” However, the term is defined in § 1.148-6(d)(4)(iii) of the Income Tax regulations (involving arbitrage bonds) as a transfer for a governmental purpose of money or property to a transferee that is not a related party to or an agent of the transferor. The transfer must not impose any obligation or condition to directly or indirectly repay any amount to the transferor.

Section 45(b)(3)(A)(ii) provides for purposes of § 45 tax-exempt bonds consist of an issue of State or local government obligations used to provide financing for the project the interest on which is exempt from tax under § 103. The proceeds of such reduce the amount of credit for any taxable year.

Section 45 does not define subsidized energy financing. However, under § 48(a)(4)(C), the term means financing provided under a federal, state, or local program a principal purpose of which is to provide subsidized financing for projects designed to conserve or produce energy.

Based solely on the representations and the relevant law and regulations set forth above, we conclude that the Advance Payment will not be considered 1) a grant provided by the United States, a state, or a political subdivision of a state for use in connection with the Project; 2) proceeds of an issue of state or local government obligations used to provide financing for the project the interest on which is exempt from tax under § 103; 3) subsidized energy financing provided (directly or indirectly) under a federal, state, or local program in connection with the Project; or 4) other credit within the meaning of § 45(b)(3)(A)(1)(iv).

Section 6.08 of Rev. Proc. 2004-1, I.R.B. 1, 15, provides that the Internal Revenue Service will not issue a letter ruling if the request presents an issue that cannot be readily resolved before a regulation or any other published guidance is issued. We have determined that the issue of whether the BETC falls within one of the categories under 45(b)(3) cannot be readily resolved before published guidance is issued. Therefore, we decline to rule on this issue.

Except as specifically set forth above, no opinion is expressed 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.

Sincerely,

Walter H. Woo  
Senior Technician Reviewer  
Branch 5  
Office of Associate Chief Counsel  
(Passthroughs and Special Industries)

cc: