

Internal Revenue Service

Department of the Treasury

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Legend

Taxpayer =

Purchaser =

Entity 1 =

Entity 2 =

Entity 3 =

Entity 4 =

SPV I =

SPV II =

a =

b =

c =

d =

e =

f =

Dear :

This is in reply to a letter dated April 4, 2005, and subsequent correspondence, submitted on behalf of Taxpayer requesting the following ruling:

That certain power supply contracts ("PSCs" collectively and "PSC" individually) and power purchase contracts ("PPCs" collectively and "PPC" individually) acquired by Purchaser are interests under an existing financial contract and are excluded from the definition of "section 197 intangible" under section 197(e)(1)(B) of the Internal Revenue Code and the regulations thereunder.

FACTS:

Taxpayer owns an a percent interest in Purchaser. Purchaser owns an a percent interest in Entity 1. Purchaser owns a b percent interest in Entity 2, and Entity 1 owns a c percent interest in Entity 2. Entity 2 owns an a percent interest in Entity 3. Entity 2 owns a c percent interest in Entity 4 and Entity 3 owns a b percent interest in Entity 4.

Taxpayer represents that Entity 1, Entity 2, Entity 3 and Entity 4 each is a disregarded entity for U.S. federal income tax purposes and is treated as a division of Purchaser because no election under section 301.7701-3 of the regulations has been made with respect to each such entity.

Pursuant to two separate Purchase and Sale Agreements, Entity 4 acquired a percent of the membership interests in two special purpose vehicles ("SPVs"), SPV I and SPV II. Taxpayer represents that each SPV has since its formation been treated as a disregarded entity not separate from its owner for federal income tax purposes because no election under section 301.7701-3 of the regulations has been made with respect to the SPVs. Based on Taxpayer representations, Entity 4 is also disregarded as an entity separate from its owner for federal income tax purposes. Thus, Purchaser is treated as having acquired all the underlying assets of each SPV, subject to their respective liabilities. The cash purchase price paid by Entity 4, as set forth in the Purchase and Sales Agreements, was d dollars and e dollars for the equity of SPV I and SPV II, respectively.

Prior to the acquisition by Purchaser of the SPVs, each SPV was a party to a PSC with a public utility, pursuant to which each SPV sold electric energy to the public utility at fixed rates that had become above-market. In addition, each SPV was also a party to a PPC pursuant to which each SPV acquired matching amounts of electric energy from another party at fixed rates that had become below market. Additionally, each SPV had issued bonds and, other than the valuable rights under the power contracts described above and certain liquidity and collection accounts held in connection with the bonds, the SPVs had no other assets. Based on Taxpayer representations that the SPVs are disregarded entities for federal income tax purposes, Purchaser would be treated as having acquired the underlying assets of the SPVs (i.e., the power contracts).

The PSCs require each SPV to supply electric energy to a public utility and requires the public utility to purchase electric energy from the SPVs. When Purchaser acquired the PSCs, there were approximately f years remaining under each PSC. The total amount of energy required to be purchased by the public utility during each calendar year and the rates to be paid to the SPV for that energy are fixed by the PSCs. The PSCs provide for delivery of energy from any source rather than from a specific output facility.

The terms of the PPCs generally mirror and correspond to the terms of the respective PSCs, except that the rates paid by the SPVs under the PPCs are substantially lower than the rates paid to the SPVs by the public utility under the PSCs.

LAW AND ANALYSIS:

Section 197(a) of the Code provides:

A taxpayer shall be entitled to an amortization deduction with respect to any amortizable section 197 intangible. The amount of such deduction shall be determined by amortizing the adjusted basis (for purposes of determining gain) of such intangible ratably over the 15-year period beginning with the month in which such intangible was acquired.

Section 197(e)(1)(B) provides that the term "section 197 intangible" shall not include any interest under an existing futures contract, foreign currency contract, notional principal contract, or other similar financial contract.

Section 1.197-2(c)(2) of the regulations provides that section 197 intangibles do not include an interest under an existing futures contract, foreign currency contract, notional principal contract, interest rate swap, or other similar financial contract, whether or not the interest is regularly traded on an established market.

In this case, the contracts at issue require the sale or purchase of electricity, a commodity with respect to which futures contracts are regularly traded on established markets. Additionally, the PPCs and the PSCs provide that the electricity supplied can come from any source, rather than requiring delivery from a specific output facility. Further, the PPCs and the PSCs are contracts that require the purchase and sale, respectively, by the SPVs of a specified amount of electricity for a specified price within a specified period.

Based on the foregoing, we conclude that the PSCs and PPCs described herein are "other similar financial contracts" within the meaning of section 197(e)(1)(B) of the Code and, therefore, are not section 197 intangibles.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter under any provision of the Code or regulations.

The rulings contained in this letter are based upon information and representations submitted by the 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 on examination.

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.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Charles B. Ramsey
Branch Chief, Branch 6
(Passthroughs & Special Industries)

Enclosures:

Copy of this letter
Section 6110 copy

cc: