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IRS Official Explains Approach in Power Generation Revenue Procedure.

The IRS chose to use a definitional safe harbor in the long-awaited power generation revenue procedure (Rev. Proc. 2013-24, 2013-21 IRB 1) because of the difficulties raised by a percentage safe harbor, Douglas E. Toney, utilities technical specialist, IRS Large Business and International Division, said during a May 16 webcast.

Issued April 30, the Service's latest industry issue resolution guidance provides safe harbor definitions for unit of property and major component that taxpayers may use when applying the disposition rules in the repair regulations (T.D. 9564) to power generation property, according to Carol Conjura of KPMG LLP, whose firm sponsored the webcast.

Conjura noted that the revenue procedure for electric transmission and distribution property (Rev. Proc. 2011-43, 2011-37 IRB 1) uses a percentage safe harbor for expensing.

"A percentage approach would have presented more challenges to implement. These are very different assets than electric and transmission distribution assets," Toney said. "The approach of defining units of property and major components is more administrable and easier to follow than a percentage approach would have been."

Conjura suggested that anticipated guidance on gas transmission property may be more likely to use a percentage safe harbor, given that gas transmission property, unlike power generation property but like electric transmission property, is considered network property.

Toney said the definitions in Rev. Proc. 2013-24 were intended to "reflect the application of the concepts in the regs to these particular and specific types of plant assets used in the generation of steam or electricity." He added that although that approach "wasn't driven by the accounting records . . . it will be easier for the power generation companies to identify these major components and units of property because of their accounting records."

Practitioner Questions

Conjura asked why the guidance didn't allow for a four-year adjustment period for a positive section 481 adjustment. According to the revenue procedure, "A taxpayer must take the entire net section 481(a) adjustment into account (whether positive or negative) in computing taxable income in the year of change."

By pushing all of the effects of section 481 into one tax year, all taxpayers will receive the same treatment, regardless of their initial positions, Toney replied.

Peter Baltmanis of KPMG LLP asked whether in the context of the guidance the definitions of different service levels contained in a taxpayer's long-term service agreement would help determine whether an expense should be capitalized or deducted. Taxpayers in the power generation industry enter into long-term service agreements that may cover the costs connected with the replacement of a major component in connection with an outage.

Although broad generalizations are difficult to make, “the long-term service agreements most likely would be one step removed from a determination of the actual work done. I don’t know that they’d be helpful,” Toney said. “The scope of the work done is probably more clearly reflected in the individual work orders.” He added that an analysis would depend on the facts and circumstances.

Acceptable extrapolation methods are contained in appendix B of the revenue procedure. Baltmanis asked about statistical sampling and whether the procedures in Rev. Proc. 2013-24 differ from those in Rev. Proc. 2011-43.

The basic principles are the same, Toney said, but “the formula was tweaked a little bit to eliminate some unintended results.” The most significant difference is that the initial calculation under Rev. Proc. 2013-24 is performed on a gross basis, not a net basis, he said.