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Courier's Desk
Internal Revenue Service
CC:PA:LPD:PR (REG-104397-18)
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Re: Proposed Regulations Under Section 168(k) (REG-104397-18)

Dear Sir or Madam:

On behalf of the Energy Tax Group of Eversheds Sutherland (US) LLP, we respectfully submit these comments with respect to proposed regulations (the "Proposed Regulations") issued on August 8, 2018, and published in the Federal Register on that same date (83 Fed. Reg. 39292) under section 168(k) of the Internal Revenue Code of 1986, as amended by Pub. Law 115-97[1] (the "Code") regarding the revised "additional first year depreciation deductions." Although our comments may have broader implications to other industries, they are principally offered from the perspective of regulated electric, gas, and water companies, many of which our firm represents in a number of capacities. Nevertheless, these comments are made not in a representative capacity, but solely to offer our suggestions on the manner in which the Proposed Regulations can be clarified and improved.

Many of the participants in the electric, gas and water industries are regulated by either state ratemaking bodies, federal ratemaking bodies, or both (hereinafter referred to for convenience as "regulated energy companies"). For regulated energy companies, it is generally true that certainty of tax treatment is of paramount importance. That is the case because although regulated energy companies are allowed to recover taxes from their customers (based upon a test year), they are generally not allowed to recover any tax shortfalls that arise if a position taken on their tax return is later successfully challenged by the tax authorities. This is commonly known as the "prohibition against retroactive ratemaking." In other words, unlike unregulated taxpayers, absent regulatory approval and subject to the prohibition against "retroactive ratemaking," regulated energy companies cannot simply raise prices to customers should they erroneously apply the tax laws. Accordingly, certainty of tax treatment takes on heightened significance for regulated energy companies seeking to comply with the tax laws.

Similarly, providing tax "elections" to regulated energy companies is not as helpful as it might superficially seem, particularly when compared to unregulated companies. Often, regulated energy companies will either be required to obtain regulatory pre-approval

[1] Pub. Law 115-97 is often referred to as the "Tax Cuts and Jobs Act" or "TCJA".

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of a tax election or, if between rate cases, must be prepared to explain to regulators after the fact how the election made was in the best interests of ratepayers. Such determinations are sometimes challenging given the competing interests of stakeholders. Consider, for example, a regulated energy company with years of accumulated net operating losses as a result of bonus depreciation, a very common fact pattern in the industry. One might have expected that those companies would have elected out of bonus depreciation to minimize the risk of net operating losses expiring under the law in effect prior to the TCJA. But very few regulated energy companies made such elections because of the potential perception that the companies were not acting in the best interests of ratepayers by choosing not to maximize available tax benefits, even though the generation of additional net operating losses by claiming additional bonus depreciation would not benefit current ratepayers.[2]

With these general principles in mind, we now turn to the various areas where the regulated energy companies would benefit from additional clarification. Our comments are divided into two main sections. First, our comments address certain aspects of the Proposed Regulations where the guidance is clear, but we believe alternative policy choices should have been made. Second, we set forth several of fact patterns that we believe are not clearly addressed in the Proposed Regulations and should be addressed in the final regulations. Again, as previously noted, although we offer our views on the appropriate treatment of these fact patterns, ultimately, having clear guidance is as important as the particular tax treatment ultimately prescribed in the final regulations.

1. Areas of Alternative Policy Choices

A. 2017 Expensing Eligibility

It is generally understood that regulated energy companies, *inter alia*, accepted ineligibility for expensing under new section 168(k) and, in return, were excluded from the interest limitation provisions under new section 163(j). Given that the effective date of new section 168(k) was September 27, 2017, prior to the issuance of the Proposed Regulations we believed, and we understand that the vast majority of regulated energy companies believed, that they would be ineligible for expensing as of that date. However, as the preamble to the Proposed Regulations correctly observes, the definition of trades or businesses excluded from expensing eligibility under section 168(k) is not contained in that subsection. Rather, it is contained in section 163(j) as amplified in forthcoming Proposed Regulations to be issued under that provision. However, the effective date of new section 163(j) was not until January 1, 2018.

In light of the inconsistent effective dates of the respective provisions, the Proposed Regulations deem property acquired by regulated energy companies after September 27, 2017 and placed in service prior to January 1, 2018 to be eligible for expensing. Although we acknowledge that the statute can be literally interpreted in this matter, we respectively submit that Treasury could and should have concluded otherwise. First, the definition of the excluded trade or business of regulated energy companies incorporated in new section 163(j) is not new. It is essentially the same definition used for purposes of the normalization provisions of the Code under sections 167, 168 and 46 and the regulations

[22] The Internal Revenue Service has frequently ruled that the deferred taxes attributable to the accelerated depreciation component of net operating losses may not be used to reduce rate base unless and until the net operating losses are used to reduce taxable income. *See, e.g.*, PLRs 201418024, 201436037, 201436038, 201438003, 201519021, 201534001, and 201548017.