

ALABAMA DEPARTMENT OF REVENUE
REVENUE RULING 99-006

This document may not be used or cited as precedent. Ala. Code ' 40-2A-5(a) (1998 Replacement Volume).

TO:

FROM: Commissioner of Revenue
Alabama Department of Revenue

DATE: December 7, 1999

RE: Applicability of Ala. Code ' 40-9B-1 et seq. and Ala. Code ' 40-18-190-203 to a taxpayer's planned facility.

FACTS

The facts as represented by the Requestor are as follows:

Corporation "A", a corporation organized and existing under the laws of the State of "X" and wholly owned by Corporation "B", plans to construct a cogeneration facility to be located within the city limits of the City of "Y" (the "Facility"). The capital investment involved is estimated to be approximately \$100,000,000. The purpose of the Facility is to provide thermal energy to one customer, Company "C". The Facility is being constructed specifically for the purpose of providing thermal energy to Company "C"'s mill in City "Y" (the "City Y Mill"). The Facility will be located on land immediately adjacent to Company "C"'s City "Y" Mill. Company "C" will provide easements for energy to be used in the production of thermal energy at the Facility, along with piping connections between the Facility and the City "Y" Mill for steam production and transmission, the return of condensate, for cooling water, firewater, potable water, and the use of Company "C" wastewater facilities.

The production of steam of the type to be manufactured by the Facility has historically been performed on-site by Company "C". For economic reasons, and because of the increased efficiency of cogeneration technology making thermal energy production more cost-effective, Company "C" has made a determination to outsource the majority of its thermal energy requirements to the Taxpayer. The decision to outsource its thermal energy needs resulted in the execution by Company "C" of contracts with the Taxpayer whereby Company "C" agrees to share certain of its facilities with the Taxpayer and lease adjacent

land owned by it to the Taxpayer at a nominal rate. But for this decision by Company "C" to outsource its thermal energy needs to the Taxpayer, the Taxpayer would not construct its facility at the proposed site in City "Y".

The production of steam is a necessary part of the Company "C"'s industrial manufacturing process. The Facility acts as an essential support facility to Company "C" in that it produces thermal energy necessary for use by Company "C" in its manufacturing process.

Thermal energy production requirements at the "Y" are dictated solely by Company "C" under the parameters of an energy services agreement. The Facility specifications, including the type, quantity and quality of thermal energy, are dictated by Company "C" alone under the terms of said energy services agreement. Company "C" is also given substantial control over other aspects of the Facility's operations via the energy services agreement, including fuel purchases and deliveries, metering and testing procedures, maintenance and repair activities, and other matters affecting the parties.

As a by-product to the production of thermal energy, electricity will be manufactured for sale to third parties. The sale of electricity will be incidental to the predominant business purpose of manufacturing steam for use by Company "C" in that the majority of the energy produced at the Facility will be in the form of steam delivered to Company "C".

ISSUES

- (1) Whether the Facility to be constructed by the Taxpayer will be considered industrial development property under Ala. Code ' 40-9B-3(5)?
- (2) Whether the Facility to be constructed by the Taxpayer will be considered an industrial, warehousing or research activity under Ala. Code ' 40-18-190(6)?

LAW AND ANALYSIS

(1) The Tax Incentive Reform Act of 1992, Ala. Code ' 40-9B-1 et seq., provides for the abatement of non-educational ad valorem taxes, construction-related transaction taxes, and mortgage and recording taxes with respect to private use industrial property. In order for property to qualify, it must be private use industrial property defined under Ala. Code ' 40-9B-3(13) as private use property that also constitutes industrial development property. Ala. Code ' 40-9B-3(5) defines industrial development property as real and/or personal property acquired in connection with establishing or expanding an industrial or research enterprise in Alabama. In turn, Ala. Code ' 40-9B-3(6) defines industrial or research enterprise as any trade or business described in 1987 Standard Industrial Classification Industry Group Number 0724, Major Groups 20 to 39, inclusive, 50

and 51, Industrial Group Number 737, and Industrial Numbers 4613, 8731, 8733, and 8734, as set forth in the Standard Industrial Classification Manual published by the United States Government Office of Management and Budget. Id. at Ala Code ' 40-9B-3(6).

The Facility will be primarily used for the production of thermal energy, an integral function of the manufacturing of paper and paper products. Major Group 26, pertaining to paper and allied products, is a major group referenced as an industrial or research enterprise in Ala. Code ' 40-9B-3(6). The predominant business activity at the Facility is the production of steam, which is an integral part of the manufacturing of paper contained in Major Group 26. But for the thermal energy demands of a single customer located immediately adjacent to the Facility, the Facility would not be constructed. The demands of thermal energy production are dictated solely by Company "C" within the parameters of an energy services agreement executed between Company "C" and the Taxpayer. Company "C" also exercises substantial control over other important decisions affecting the Facility's operations. Based on the facts presented, the Taxpayer's planned facility falls within a Major Group specified in Ala. Code ' 40-9B-3(6).

(2) Ala. Code ' 40-18-192 provides that [s]ubject to compliance with Section 40-18-193, each investing company shall, upon filing of the statement required by Section 40-18-191 and upon the making of qualified investments and upon compliance with subsection (a) of Section 40-18-193, be entitled to the capital credit, such credit to be allocated and available in accordance with subsection (b) of Section 40-18-194. Section 40-18-190(11) defines a qualifying project as one in which the capital costs are not less than \$2,000,000 and the predominant trade or business activity conducted will constitute an industrial, warehousing or research activity. Section 40-18-190(6) defines an industrial, warehousing or research activity as any trade or business described in 1987 Standard Industrial Classification Major Groups 20 to 39, inclusive, 50 and 51, Industrial Group Number 737, and Industrial Numbers 4613, 8731, 8733, and 8734, as set forth in the Standard Industrial Classification Manual published by the United States Government Office of Management and Budget. . . .

For the reasons described in (1) above, the Taxpayer's activity conducted at the planned facility falls within a Major Group specified in Section 40-18-190(6).

HOLDING

(1) Taxpayer's planned facility qualifies as an industrial or research enterprise as defined in Ala. Code ' 40-9B-3(6). The property and equipment to be acquired as well as any construction to be accomplished for the Facility is for the purposes of establishing this enterprise. Therefore, said real and personal property is industrial development property.

(2) Taxpayer's predominant trade or business activity conducted at its planned Facility constitutes industrial, warehousing or research activity as defined in Ala. Code ' 40-

18-190(6). The property and equipment to be acquired as well as any construction to be accomplished for the Facility is for the purposes of establishing this enterprise, and, provided that the other requirements of Ala. Code ' 40-18-190(11) are met, the Facility will meet the definition of a qualifying project..

JAMES P. HAYES, JR.

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