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Opinion No. 02-080

Determination of Payments in Lieu of Taxes by McMinnville Electric System

QUESTIONS

1. Should the generation facility constructed by McMinnville Electric System ("MES") to maintain and perform contractual obligations under agreements with the Tennessee Valley Authority ("TVA") be included in the calculation of the "net plant value" of MES for purposes of determining the payments in lieu of taxes on property and operations owed to McMinnville and Warren County, Tennessee, by MES pursuant to Tenn. Code Ann. § 7-52-301 *et seq*.?

2. Is McMinnville Electric System entitled to a credit from McMinnville and Warren County for the amounts already paid pursuant to Tenn. Code Ann. § 7-52-301 *et seq*., which amounts include an increase of $96,072.55 because of the inclusion of the generation facility in the calculation of the "net plant value"?

OPINIONS

1. Yes. Based on the facts provided, the generation facility constructed by MES to maintain and perform contractual obligations under agreements with the TVA should be included in the calculation of "net plant value" of MES for purposes of determining the amount of payments in lieu of taxes on property and operations owed to McMinnville and Warren County by MES pursuant to Tenn. Code Ann. § 7-52-301 *et seq.*

2. No. The McMinnville Electric System is not entitled to a credit from McMinnville and Warren County for the amounts already paid pursuant to Tenn. Code Ann. § 7-52-301 *et seq.*

ANALYSIS

1. Calculation of "Net Plant Value" for Determining Payments in Lieu of Taxes

According to the information provided in your opinion request, MES constructed a facility to generate electricity ("the new generation facility"). This generation facility was constructed pursuant to a contract between MES and the TVA that requires MES to generate electricity that it then delivers to the TVA's transmission system or to other facilities as the TVA directs. MES is not allowed to use this facility to generate any electricity for its own use without permission from the TVA. MES has delivered all electricity generated by this facility to the TVA's transmission system pursuant to its contractual agreements. MES has not produced any electricity for its own use apart from the TVA system.

The relevant law is Tenn. Code Ann. § 7-52-301 *et seq.* Specifically, Tenn. Code Ann. § 7-52-304 addresses the calculation of the amount for payments in lieu of taxes ("tax equivalents") on the property and operations of all electric systems owned and operated by incorporated cities or towns, by counties, and by metropolitan governments. Under § 7-52-304, the total amount of tax equivalents for each fiscal year shall not exceed a maximum amount as calculated by applying the rules contained in that section. Part of the initial calculation includes calculating the net plant value of the electric plant as defined in Tenn. Code Ann. § 7-52-303(8).

Under Tenn. Code Ann. § 7-52-303(8)(A), net plant value includes the depreciated original cost of the electric plant that is in service, the part held for future use, and the book value of any construction work in progress, all as shown on the electric system's books and all of which the electric system uses to generate, transmit and distribute electricity. However, under Tenn. Code Ann. § 7-52-303(8)(B),

> For purposes of subdivision (8)(A): (i) "Electric plant" does not include that portion of any electric system properties that a municipality owns, operates, and maintains to perform contractual obligations, under agreements with the Tennessee valley authority, requiring the municipality to: (*a*) Take the net output of a specified generating facility of the Tennessee valley authority into the municipality's electric system; and (*b*) Deliver all or portions of such net output to the transmission system of the Tennessee valley authority or to other electric facilities as specified by the Tennessee valley authority...

Under the facts provided, MES does not meet the requirements of Tenn. Code Ann. § 7-52-303(8)(B) because, in order for the new generation facility to be exempt from the net plant value calculation, that facility would have to be **both** receiving the net output of a specified generating facility of the TVA into its electric system as specified in Tenn. Code Ann. § 7-52-303(8)(B)(i)(*a*), **and** also delivering all or portions of such net output to the TVA's transmission system or to other facilities as the TVA directs (Tenn. Code Ann. § 7-52-303(8)(B)(i)(*b*)). MES does not do either of these things. MES

uses the new generation facility (which is owned by MES, and thus is not a generation facility of the TVA) to generate electricity that it then sells to the TVA under the terms of its contract.

As a matter of principle, Tenn. Code Ann. § 7-52-303(8)(B) provides that when a contract requires a municipality to use its own transmission facilities to take and deliver the net output of a TVA plant, then those facilities shall not be included in determining its payments in lieu of taxes. This does not describe the instant situation, however. Here the plant is owned by the municipality. The municipal transmission facilities are not being used to take or deliver power from a TVA plant; rather, they are being used to deliver power generated by a municipal plant. The exclusion in the statute simply does not describe the situation set forth in the request letter and accompanying contract.

Since MES does not meet the requirements under Tenn. Code Ann. § 7-52-303(8)(B), MES must include the new generation facility when calculating its total net plant value for purposes of determining the amount to be paid as tax equivalents to McMinnville and Warren County.

2. Entitlement to Credit

The information provided indicates that MES made tax equivalent payments to McMinnville and Warren County for the 2002 fiscal year and that those amounts were determined by including the new generation facility in the net plant value. If the calculations were made as stated, then it would follow that MES is not entitled to a credit from McMinnville and Warren County because the new generation facility was properly included in the net plant value.

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