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SALT RIVER PROJECT

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FEDERAL EXPRESS

Regulatory Publications Branch, DFIPS
Office of Administration and Resources Management
U.S. Nuclear Regulatory Commission
Washington, D.C. 20555

RE: Draft Regulatory Guide on Assuring the Availability
of Funds for Decommissioning Nuclear Reactors

Ladies and Gentlemen:

This letter responds to the U.S. Nuclear Regulatory Commission (the "NRC") Office of Nuclear Regulatory Research request for public comment on the Draft Regulatory Guide On Assuring The Availability Of Funds For Decommissioning Nuclear Reactors (the "Draft Guide"). These comments have been prepared on behalf of Salt River Project Agricultural Improvement and Power District ("SRP"), a participant in the Arizona Nuclear Power Project ("ANPP"), also known as the Palo Verde Nuclear Generating Station ("Palo Verde"). Palo Verde is an electric generating plant composed of three units, located approximately 55 miles southwest of Phoenix, Arizona. The other participants in Palo Verde are Arizona Public Service Company, Southern California Edison Company, Public Service Company of New Mexico, El Paso Electric Company, Southern California Public Power Authority, and the Department of Water and Power of the City of Los Angeles.

Certain participants in the ANPP, including SRP, have submitted their joint comments on the Draft Guide ("ANPP Comments"). SRP generally concurs with these comments. However, SRP, as a political subdivision of the State of Arizona, has some concerns which differ from those of the other participants and, accordingly, has limited the extent of its joining in the ANPP Comments. This letter consists of comments and concerns particular to SRP.

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I. Taxability of Sinking Fund Trust.

SRP, as a political subdivision of the State of Arizona, is not subject to federal income taxation. Paragraph 2.5 of the Draft Guide provides that certain governmental agencies are permitted to satisfy the funding requirements by submitting a statement of intent that contains specified provisions. A Federal, State or local licensee which is not an "electric utility" may submit a statement of intent. 10 CFR 50.75(e)(2)(iv). However, an "electric utility," as defined in 10 CFR 50.2, may only utilize the statement of intent method if it is a Federal government licensee. 10 CFR 50.75(e)(3)(iv). Because SRP is an "electric utility" and is not a Federal government licensee, it apparently may not satisfy the funding requirements of 10 CFR 50.75(e) by submitting a statement of intent. Consequently, unless and until the regulations or the interpretation thereof change, SRP will establish an external sinking fund trust as authorized by 10 CFR 50.75(e)(3)(ii).

Appendix A to the Draft Guide defines a "Trust Fund" as an irrevocable three party agreement consisting of the licensee, a trustee, and the beneficiary. The beneficiary is defined to be either the NRC or a state agency. We question the necessity and purpose of requiring the NRC or a state agency to be the beneficiary of the decommissioning trust. We believe that the beneficiary of the trust should be the licensee of the nuclear reactor, the party who is responsible for decommissioning.

The ANPP Comments recommend the deletion of the requirement that a sinking fund trust be irrevocable. In addition, the AANP Comments recommend that the licensee, and not the NRC or a state agency, be the trust beneficiary. We agree with these recommendations and the rationale of the ANPP Comments. However, as a political subdivision, we have additional reasons for supporting these recommendations, which are addressed herein.

SRP would not pay income tax on earnings from funds held for decommissioning if it were permitted to hold the funds internally as it now is doing. However, because the funds will be held in an external sinking fund (a separate entity for tax purposes), the income from such funds will not necessarily be exempt from taxation. Because of the significant funds involved, SRP is preparing an application to the Internal Revenue Service

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("Service") for a private letter ruling ("Ruling") that income from the decommissioning funds held in the trust will be exempt from taxation.

Generally, income from a trust is taxable, even if the grantor is an entity exempt from taxation. However, there are two theories on which the income from an external sinking-fund trust could be exempt from taxation. First, if the trust is a "grantor trust," the grantor will be taxed as if it owned the trust assets directly. Second, trust income may be excluded from gross income under I.R.C. § 115. This section excludes from the definition of gross income any income derived from a public utility or derived from the exercise of an essential governmental function which accrues to a state or political subdivision thereof. Both these theories are generally inconsistent with a three-party trust in which anyone other than the grantor is the beneficiary, and are specifically inconsistent with the recommended trust language in the Draft Guide.

A. Grantor Trust.

1. NRC as Beneficiary.

Under I.R.C. § 677, the grantor is treated as the owner of any portion of a trust whose income, without the approval or consent of any adverse party, is or may be distributed to the grantor or held or accumulated for future distribution to the grantor. In addition, the grantor is treated as the owner of a trust whose income is, or, in the discretion of the grantor or a nonadverse party, or both, may be applied in discharge of a legal obligation of the grantor. Treas. Reg. § 1.677(a)-1(d). For these purposes, the term "adverse party" means any person having a substantial beneficial interest in the trust. Treas. Reg. § 1.672(a)-1(a). Treasury regulations also provide that a beneficiary is ordinarily an adverse party. Treas. Reg. 1.672(a)-1(b).

Although SRP is confident of its analysis with respect to the tax aspect of a properly structured trust, there is no existing authority directly on point. SRP is concerned that it may not be able to obtain a favorable Ruling using a three-party trust with the NRC or a state agency as the beneficiary. In addition, the draft trust agreement provides in section 5 that the trustee may only make payments from the trust fund to the

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grantor upon presentation of a certificate to the trustee, and after 30 days prior notice has been given to the NRC. Moreover, the NRC must approve the withdrawal of funds exceeding a certain percentage or dollar amount. Because the interest of the NRC or state agency as beneficiary may be deemed to be adverse to SRP, the Service may hold that the decommissioning trust is a separate taxable entity. As such, the trust would be required to pay tax on the sinking fund earnings which tax would not be required to be paid if SRP held the funds internally, or if the funds were held in a trust classified as a grantor trust.

In order to obtain a favorable Ruling, we believe it is necessary that SRP be the sole beneficiary of the trust. In addition, it is necessary that we retain flexibility to modify the trust language to satisfy requirements of the Service with respect to our Ruling request.

We believe that the NRC is adequately protected by current regulations, and that it is not necessary for the NRC (or a state agency) to also be the beneficiary of the decommissioning trust. We also believe that the beneficiary of a decommissioning trust should be the licensee, the party who is directly responsible for decommissioning. Furthermore, the NRC would indirectly benefit if SRP's sinking fund trust were not subject to taxation because more funds would thus be available for decommissioning.

2. Irrevocability of Trust.

Section 16 of the draft trust agreement states that the trust shall be irrevocable. As stated in the ANPP Comments, we believe the NRC is already adequately protected and there should not be a requirement that the trust be irrevocable. Furthermore, subparagraph 2.1.6.1 of the Draft Guide contemplates that a licensee may change the funding method during the life of the facility. However, a licensee utilizing a sinking fund trust may be effectively precluded from changing funding methods if the trust must be irrevocable. This would result in less favorable treatment (less flexibility) to a licensee who initially elected to use a sinking fund trust. Consequently, because of the need to permit licensees to change funding methods, and because the interest of the NRC will not be adversely affected, we believe that a external sinking fund trust should, at the option of the licensee, be revocable.

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B. I.R.C. § 115.

Another theory by which SRP may be able to obtain a favorable Ruling is based on I.R.C. § 115. As stated previously, I.R.C. § 115 provides that trust income does not include "income derived from any public utility or the exercise of any essential governmental function and accruing to a State or any political subdivision thereof. . . ." While we believe that the decommissioning trust would be performing an essential governmental function, it is questionable whether the income of the trust "accrues" to SRP under the form decommissioning trust contemplated by the Draft Guide.

A decommissioning trust is formed by the licensee, under the supervision of the NRC, for the purpose of ensuring that adequate funds will be available to the licensee to satisfy its legal obligation of decommissioning a nuclear reactor. However, the recommended wording for the trust states in section 3 that the trust fund is established for the benefit of the NRC. We are concerned, under the trust agreement in the Draft Guide, that the Service may rule that I.R.C. § 115 does not apply to the decommissioning trust because the income from such trust does not accrue to SRP.

The NRC is not responsible for the actual decommissioning of a nuclear reactor, but, rather, its capacity is supervisory in nature. Declaring the NRC or a state agency to be the beneficiary of the trust would make it appear as if the NRC or state agency is the party responsible for decommissioning. Because we believe the NRC's interest are adequately protected by the regulations, and because of our need to obtain a favorable Ruling from the Service, we believe that the beneficiary of the decommissioning trust should be the licensee, and that the trust specify that funds from the trust are to be used to satisfy the licensee's legal obligation of decommissioning.

II. I.R.C. § 468A

I.R.C. § 468A sets forth various requirements and restrictions which, if satisfied and if the taxpayer so elects, will result in favorable tax treatment to a taxable licensee with respect to a decommissioning fund. SRP, as a political subdivision exempt from taxation, does not need or want, and may

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be adversely affected by, the restrictive language of I.R.C. § 468A in its trust agreement. Consequently, it would oppose any required language with respect to the provisions of I.R.C. § 468A.

III. Required Language for Trusts.

We believe that the Final Guide should not include required language for a trust agreement used to satisfy the funding requirements. Standardized language is not necessary, would be unduly restrictive, and would be impossible to draft without including multiple alternative provisions. This is because:

A. Each trust agreement will be governed by the laws of a particular state. It would be difficult to design a trust agreement which complies with the laws of 50 different states;

B. Trustees often require special or unique provisions because of the nature of their organization or because of an experience or problem which they have encountered in the past; and

C. As discussed previously, some licensees will desire language satisfying the requirements of I.R.C. § 468A, while other licensees will find the I.R.C. § 468A restrictions unnecessary and unacceptable.

IV. Conclusion.

As previously stated, we generally concur with the conclusions and recommendations set forth in the ANPP Comments. We have supplemented the ANPP Comments with respect to the additional concerns and recommendations we have arising from our unique nature.

For the reasons set forth above, it is our recommendation that the NRC not attempt to structure a standardized decommissioning trust form. We believe that NRC is adequately protected by existing regulations, and that the disadvantages of required language far outweigh any benefit to be derived therefrom.

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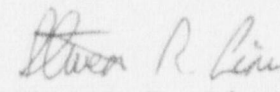
Specifically, with respect to characteristics of a decommissioning trust, we believe that the licensee should be given the discretion to structure the trust as either revocable or irrevocable. In addition, we recommend that the beneficiary of the trust be the licensee rather than NRC or a state agency.

We hope that the NRC will find these comments useful. If you have any questions or would like to discuss any aspect of these comments further, please feel free to telephone the undersigned at (602) 236-5553 at anytime.

Very truly yours,

SALT RIVER PROJECT

By



Steven R. Linn

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