

Congress of the United States
Washington, DC 20515

December 11, 2015

The Honorable John Koskinen
Commissioner
Internal Revenue Service
1111 Constitution Avenue NW
Washington, DC 20224

The Honorable Mark Mazur
Assistant Secretary (Tax Policy)
Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

Dear Commissioner Koskinen and Assistant Secretary Mazur:

We are writing to urge the Internal Revenue Service to resolve an important tax matter relating to water conservation and stormwater management. Many water utilities have programs to encourage private property owners to make water efficiency and stormwater-related improvements and are providing rebates to defray the property owner's cost. The IRS should issue a revenue ruling clarifying that these rebates are not taxable both because they are fundamentally a reduction in purchase price and because they are not intended to confer a net benefit on the private property owner.

Severe droughts and a growing awareness of limited freshwater resources are driving communities across the nation to cut water usage. Encouraging residents to reduce water usage by replacing water-thirsty lawns, installing "gray water" capture systems, or purchasing new water-efficient appliances can provide significant water savings. However, these improvements are often too expensive for property owners to install without a financial incentive. To encourage more installations, water utilities have established programs to provide rebates to defray costs.

Protecting our waterways from stormwater runoff pollution is critical for public health, local economies, and our environment. Because so much of the natural surface in our cities is paved over, rainwater is no longer able to soak directly into the ground. Instead, rainwater flows over city streets, collecting a range of pollutants, such as motor oil, antifreeze, and pesticides, before entering into local water bodies. In older cities with "combined" sewer systems, stormwater runoff mixes with wastewater containing raw sewage and can overflow into local waterways. Approximately ten trillion gallons of polluted stormwater runoff impairs our rivers, lakes, and oceans each year, making stormwater runoff a significant cause of water pollution. Dealing with this issue is not only a matter of good governance, but is required by the Clean Water Act.

Rather than just building more and more wastewater treatment plants, sewers, and pipes, water utilities have increasingly turned to “green infrastructure,” such as rain gardens, green roofs, cisterns, planter boxes and permeable pavement. These infrastructure solutions are designed to retain stormwater at or near the site where it falls, rather than route all stormwater to overburdened centralized infrastructure. As much of urban land is privately owned, many local water utilities have established green infrastructure rebate programs to encourage private property owners to install green infrastructure on privately-owned land.

When water conservation and green infrastructure rebate payments are taxable to the property owners who receive them, it significantly deters participation in these programs. Fortunately, Treasury and the IRS have ample authority under current law to address this issue. The rebates should be nontaxable because they are fundamentally a reduction of the purchase price of the water conservation or green infrastructure installation (analogous to manufacturers’ rebates paid to customers who buy automobiles from car dealers). Support for this conclusion can be found in Revenue Ruling 76-96, 1976-1 C.B. 23, suspended in part on another issue; as well as Revenue Ruling 2005-28, 2005-1 C.B. 1997; Revenue Ruling 88-95, 1988-2 C.B. 28, further clarified by Revenue Ruling 2001-8, 2001-1 C.B. 726; *Freedom Newspapers, Inc. v. Commissioner*, 36 T.C.M. 1755 (1977); *James Brown v. Commissioner*, 10 B.T.A. 1036 (1928).

Additionally, the rebates should be nontaxable because the benefit of the water conservation or green infrastructure installation goes to the water utility (by reducing demand for potable water or reducing local costs for stormwater management). *See also* Letter Ruling 7950049 (Sep. 12, 1979). Municipal water conservation and green infrastructure rebate programs are not intended to confer a net benefit on the property owner as most benefits are not expected to exceed out-of-pocket installation and maintenance costs.

Thank you for your consideration of this important matter. We look forward to your timely response.

Sincerely,



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MEMBER OF CONGRESS



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