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Q&A Section 1603 Safe Harbor Scenarios

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Question 1: If a developer follows the safe-harbor guidelines for assets to be used in a renewable energy project, but ultimately that specific project cannot be completed, can the developer use the "safe-harbored" assets for another project and still qualify for a Section 1603 cash grant payment?

Answer 1: Yes. The developer should be able to use the safe-harbored assets as part of another project and the second project will qualify for a Section 1603 payment, assuming all other program requirements are satisfied.

The Payments for Specified Energy Property In Lieu of Tax Credits program (commonly referred to as the Section 1603 cash grant exchange program) is scheduled to sunset on December 31, 2011. However, renewable energy projects that meet the safe-harbor requirements of the Section 1603 program guidance and are placed in service prior to the applicable credit termination date for the applicable type of equipment are still eligible for Section 1603 payments. (For additional information, please see this month's 'The Current' by Forrest Milder on page 68.)

Assume that on December 15, 2011, a developer makes a non-refundable deposit of $500,000 on a wind turbine pursuant to a turbine supply contract with a manufacturer (Turbine A). The developer intends to use the wind turbine for a wind facility, Facility A, which is expected to be placed in service prior to the credit termination date for wind facilities of December 31, 2012. On February 15, 2011, the developer receives title to the wind turbine and takes delivery of the wind turbine by storing it in a warehouse near the proposed site of Facility A. The total cost of Facility A eligible for a Section 1603 payment is estimated to be $5 million; thus, the non-refundable deposit represents 10 percent of the estimated cost of Facility A.

Have a question on the Renewable Energy Tax Credit Program? We encourage you to submit questions for the monthly Q&A column. Questions can be submitted to cpas@novoco.com

During January 2012, the host customer for Facility A, a commercial enterprise that previously committed to purchasing the electricity from Facility A pursuant to a power purchase agreement (PPA), pulls out of the transaction by canceling the PPA. The developer is also in the process of developing a second wind facility, Facility B, and decides to use Turbine A as part of this wind facility.

Question and Answer 20 of the Department of the Treasury's "Frequently Asked Questions – Beginning of Construction" document specifically discusses a scenario in which a developer enters into a contract for the manufacture of certain assets and subsequently assigns the rights to such assets to an affiliated special purpose vehicle. Also, a quick look at Section 2B of the "Sample Begun Construction Application" on Treasury's web site shows that an applicant is not required to state the location of the project. In the example above, the developer has "begun construction" of a renewable energy project by making the nonrefundable deposit prior to December 31, 2011, and taking delivery of the wind turbine within three and one-half months from the date of payment. As long as all other requirements of the Section

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1603 program are satisfied, the change in project site should not affect Facility B's eligibility for a Section 1603 payment.

Question 2: If a solar developer satisfies the safe-harbor guidelines using a specific batch of equipment purchased during 2011, but ultimately uses a different batch of equipment purchased subsequent to 2011 for a solar facility, is the project eligible for a Section 1603 cash grant payment?

Answer 2: No. Because the final costs incurred for the project do not include assets safe-harbored in 2011, the solar facility is not eligible for a Section 1603 payment. But, assuming the solar project is placed in service prior to December 31, 2016, the owner of the solar project would be eligible for investment tax credits.

Assume a solar developer has purchased $750,000 of solar panels (Batch A), pursuant to a non-refundable contract, for a photovoltaic solar facility that is estimated to include eligible costs $10 million (Facility S). The developer takes title to Batch A within three and one-half months from the date payment was made. During 2012, prior to completing Facility S, the developer is able to procure more efficient solar panels for the same price as Batch A, $750,000, that will generate more electricity and thus make the project more profitable (Batch B). The developer no longer wishes to use the panels in Batch A and would prefer to use the panels in Batch B. Assume that the developer has not made any additional payments related to equipment for Facility S prior to December 31, 2011.

If the developer completes Facility S using Batch A, Facility S will have total eligible costs of $10 million, including $750,000 (7.5 percent) of costs that were safe-harbored. Assuming all other program requirements are met, Facility S would be eligible for a Section 1603 payment. However, if Batch B is used instead of Batch A, none of the $10 million of eligible costs of Facility S will have been safe-harbored for purposes of the Section 1603 program and Facility S will not be considered to have begun construction.

Novogradac & Company hosted a webinar on September 22 in association with Chadbourne & Parke LLP and Nixon Peabody LLP, to discuss safe harbor strategies for the Section 1603 Program and other pertinent program rules. This webinar is available for download at www.novoco.com/products. ❖

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