Novogradac 2017
Financing Renewable Energy Tax Credits Conference
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Discussion of Current Issues
Tax Practitioners Roundtable

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Discussion Topics

• Placed-in-service issues – Robert Dodson
• Valuation issues – Forrest Milder
• Back-leveraged debt versus direct debt – Scott DeMartino
• Start of construction and transition issues – Amanda Rosenberg
• Economic substance with inverted leases – Jerry Breed
Placed-In-Service

• Importance of Placed-in-Service to Renewable Energy Incentives
  – Determines Year to Claim Investment Tax Credit and Depreciation
  – Tax Credit Equity Investor Must be in Ownership Position Prior to Placed-in-Service
• Determining when property is Placed-in-Service
  – 5 factors/Case Law/IRS Guidance
• Placed-in-Service Example
• Questions
Placed-In-Service

• Determining when property is “placed-in-service”
  – The earlier of:
    • The year in which under the taxpayer's depreciation practice, the period for depreciation with respect to such property begins; or
    • The property is in a condition or state of readiness and availability for its specifically assigned function.
  – 5 Factors: IRS and the courts look to five factors, none of which are dispositive, in evaluating whether qualified energy property is ready and available for its specifically assigned function
    1. Approval of required licenses and permits;
    2. Passage of control of the facility to taxpayer;
    3. Completion of critical tests;
    4. Commencement of daily or regular operation; and
    5. Synchronization to the power grid for generating electricity to produce income.
Placed-In-Service

• Determining when property is “placed-in-service”
  – Case Law
    • Sears Oil Co. v. Commissioner, 359 F.2d 191 (2d Cir. 1966)
    • SMC Corp v. United States, 675 F.2d 113 (6th Cir. 1982)
  – IRS Guidance
    • Treasury Regulations
      – 1.46-3(d)(2)(i)
      – 1.46-3(d)(2)(ii)
    • Revenue rulings
      – Rev. Rul. 76-256
      – Rev. Rul. 76-428
    • Private letter rulings
      – Wind (PLR 201311003)
      – Solar (PLR 201326008)
Placed-In-Service

• Deal Structuring and “Placed-in-Service” Issues
  – Front-end structuring
    • Language consistency throughout documents
    • Realistic time frames for construction/utility connection
  – Determining Placed-In-Service
    • Delays outside of the taxpayers control
    • Review of project documents (PPAs, EPCs, etc.)

• Placed-In-Service Example
Valuation Issues – 1

• When is valuation important?
  – Justifying the purchase price (and the credit) in a single tier transaction
  – Setting the value (and the credit) in an inverted lease transaction
  – Setting the buyout price for the equipment or an interest; this can matter when determining whether tax equity is a real owner, and for tax-exempt use questions, see Section 7701(e)(3) and (4).
Valuation Issues – 2

• What are the valuation methodologies?
  – Actual Cost
  – Comparable sales
  – Capitalization of Income
Valuation Issues – 3

• The Hot Issues –
  – Role of Appraisals, and the three factors.
  – Is a development fee appropriate? How much?
  – In the capitalization method, what portion of the value is attributable to the PPA or “going concern”? E.g., two identical facilities, one with a AAA off-taker, and the other with a lower credit rating – is the first worth a larger credit?
Valuation Issues – 4

• Law and Authorities
  – Treasury Rule in 1603 program (“Evaluating Cost Basis for Solar Photovoltaic Properties”)
  – IRS PLRs – PLR 201214007 included PPA, then 201249013 withdrew the prior ruling.
  – Alta Wind Case (Ct Claims 2016) – Very supportive of taxpayer’s position.
Back-Leveraged vs. Direct Debt

- Sponsor Parent
- Sponsor Holdco
- Tax Equity Partnership
- Project Company
- Tax Equity Investor

Back-Leverage/Holdco Loan
Construction/Perm Loan
Back-leveraged vs. direct debt

• 70%-80% of Project Cost
  – plus tax and sponsor equity

• Tax Concerns
  – Basis
  – To DRO or not to DRO
  – Cash traps, sweeps and preferred distributions
  – Gain on exit
Back-leveraged vs. direct debt

• Business Concerns
  – Lender security/hybrid?
  – Change of control provisions/removal
  – Lender consent
Start of Construction

• Wind projects had to be under construction by the end of last year to qualify for 100% PTCs.

• The levels are 80% for projects starting construction in 2017, 60% in 2018 and 40% in 2019.
Start of Construction

• Solar projects that are under construction by December 2019 will qualify for a 30% investment tax credit. The credit will fall to 26% for projects starting construction in 2020 and 22% for projects starting construction in 2021.

• Projects that are under construction before these deadlines must be placed in service by December 2023 to qualify.

• The investment credit will revert to its permanent 10% level after 2021.
Start of Construction


- 5% Test
  - Paying vs. incurring costs
- Physical Work of a Significant Nature
  - On site vs. factory work

Binding contracts
Continuous efforts/construction (safe harbor)
Economic Substance for Inverted Leases

The Space Between

I. Revenue Procedure 2014-12 (historic) and Revenue Procedure 2007-65 (wind)

II. A Place for Puts and Calls?

III. Variability in cash flow is required in inverted lease transactions
Economic Substance for Inverted Leases

Variability Encompasses

I. No artificial fees
II. No sponges in the Master Lease Rent
III. No mid-course “sculpting” that “trues up” the projected cash flows