Portfolio Media. Inc. | 860 Broadway, 6th Floor | New York, NY 10003 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

New Tax Credit Timeline Will Give Wind Industry A Leg Up

By **Keith Goldberg**

Law360, New York (September 23, 2013, 7:16 PM ET) -- The Internal Revenue Service said Friday that renewable energy projects that are up and running by the end of 2015 won't need additional reviews to qualify for popular tax credits, providing some much needed certainty on the incentive that will particularly boost wind project developers' efforts to secure financing from skittish investors, experts say.

Clarifying April guidance in which it stated that certain renewable energy projects would be eligible in 2014 for the production tax credit — or alternatively, the energy investment tax credit — if developers start significant physical construction work this year or spend more than 5 percent of the project's total cost in 2013, the IRS said that developers wouldn't have to show continuous efforts toward construction work after this year to stay eligible for the credit as long as the projects were in service by Jan. 1, 2016.

Jeff Davis, a Mayer Brown LLP tax partner and co-head of the firm's renewable energy group, calls the two-year safe harbor "a huge win for the industry."

"It will give investors the comfort they need, so developers won't have to give a guarantee or indemnity in order to secure financing," Davis told Law360 on Monday. "As a result, developers will be more inclined to move ahead on projects, especially those where there might not be a clear path to completion but where the developer is confident it can complete the project by the end of 2015."

Since it was first enacted in 1992, the production tax credit has been a boon to wind developers, which say it has helped the industry become commercially viable. The energy investment tax credit, a production tax credit alternative first mandated in 2009, provides an incentive equivalent to 30 percent of the initial cost of wind, solar and fuel cell systems, or 10 percent of the cost of geothermal, microturbine and so-called combined heat and power systems.

While the wind industry cheered the IRS' April guidance — especially given the uncertain future of the tax credits, which are set to expire at year's end — it was unsure of how to deal with the IRS' continuous construction test, even though it allows for certain exemptions such as if the project is hit by a natural disaster, labor stoppages or permitting delays.

"Let's say you're building a wind farm and you tell your construction crew to take two months off for some reason. Did you continuously construct?" Akin Gump Strauss Hauer & Feld LLP tax partner David Burton said. "People are worried about that type of thing: What does 'continuous' mean?"

With banks and tax equity investors already leery about financing renewable energy projects, a subjective standard on what qualifies as continuous construction makes them even more hesitant to sink cash into a project, experts say.

"If there were going to be any delays, or potential delays, then that created uncertainty," said David Lowman Jr., who co-chairs Hunton & Williams LLP's global renewable energy practice group. "The investors in these types of projects don't like uncertainty."

That puts pressure on developers to have all their ducks in a row: a construction schedule, the ability to manage pauses in construction and documentation supporting those decisions, power purchasing agreements, to name a few.

"You had developers wringing their hands, saying, 'Am I going to meet this test; am I going to be audited?'" Burton said.

The IRS ruling provides a clear timeline: As long as you start work by year's end and finish it by the end of 2015, you'll get the tax credit without being subject to significant second-guessing by the agency.

"If you've got folks that are starting physical construction and have a plan to continue that construction, and things happen to interrupt it, those would have been fine," Lowman said. "Where it's big is in the deals that aren't to that stage, where [developers are] still out negotiating out the terms of the transaction. Those are the folks that are going to be really helped by this."

Another IRS clarification announced Friday that will reassure investors and developers is that a project's construction start date and resulting tax credit are project-specific, not taxpayer-specific, experts say. That means even if a qualified project changes hands or acquires investors, the new investors will still enjoy the tax benefits, something that was unclear in the IRS' April guidance.

Without that reassurance, projects may have had trouble attracting investors, experts say.

"You can see an example where a developer is out there taking a lot of work to develop the project but doesn't have the financial wherewithal to complete it," McDermott Will & Emery LLP energy tax team leader Phil Tingle said. "You can bring a financial player into the deal — it would be a ready source of capital that wouldn't be available [without the tax credit]."

If April's guidance from the IRS spurred developers to break ground on new wind projects by year's end, they're going to be equally spurred by Friday's guidance to finish their projects by the end of 2015, experts say.

"The IRS is just saying, 'Listen, between the point of identifying something and having it built, two years is kind of the sweet spot for one of those projects,'" Tingle said. "As a practical matter, people are going to want to get this done by Jan. 1, 2016."

The new guidance also reaffirms the Obama administration's commitment to encouraging renewable energy development, experts say.

"By issuing this guidance, they're essentially signaling that they're listening to the industry and that they want to be responsive," Davis said.

--Additional reporting by Natalie Rodriguez. Editing by Elizabeth Bowen and Katherine Rautenberg.