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Tax Credit Eligibility Boost Puts Wind In Developers' Sails

By **Keith Goldberg**

Law360, New York (May 10, 2016, 6:12 PM ET) -- The Internal Revenue Service's recent doubling of the time clean energy developers have to complete projects in order to qualify for the renewable production tax credit lowers risks for both developers and investors, and will translate to more green projects being launched and completed, experts say.

With Congress enacting a multiyear extension of the PTC in December as part of a $1.15 trillion budget deal, the IRS issued updated eligibility guidance for the tax credit last week. The centerpiece of the updated guidance was extending the so-called continuity safe harbor from two years to four years. It's the time window developers have from starting construction of their projects to finishing them in order to qualify for the PTC without having to prove they were continuously constructing the projects.

Given that it often takes 18 to 24 months to develop and complete an onshore wind project, the four-year safe harbor will provide some breathing room for developers, as well as more certainty for jittery project investors, said Mayer Brown LLP tax partner Jeff Davis, the co-head of the firm's renewable energy group.

"Investors are pretty reluctant to finance a transaction where there are gaps in construction, pauses or other things," Davis said. "Stretching the safe harbor from two years to four years gives developers a lot more time to complete their projects without having to demonstrate continuous work. If necessary, they could even put a project on ice for several months if they needed to dedicate resources to something else."

The PTC was extended for five years, with developers able to claim the full credit as long as they begin construction of their project by the end of 2016. That decreases to 80 percent of the credit in 2017, 60 percent in 2018 and 40 percent in 2019 before expiring.

It was the latest in a flurry of annual, retroactive extensions enacted by Congress, extensions that had forced the IRS to keep pushing back the expiration of the two-year safe harbor. Under the new guidance, the IRS is giving developers a finite window to complete their projects, regardless of any future actions by Congress, according to Stoel Rives LLP partner Greg Jenner, a former head of the U.S. Department of the Treasury's Office of Tax Policy.

"It's a way for the IRS to get themselves out of a little box which they had created for themselves," Jenner said.

Under the previous two-year safe harbor, all wind projects would have to have been completed by December 2018 in order to qualify for the full PTC. Now, developers that start construction of their projects this year — either by starting physical work of a significant nature or spending at least 5 percent of the project's total cost — have until the end of 2020 to complete them.

Not only will the four-year safe harbor allow more onshore wind projects to get off the ground and qualify for the PTC, but it could also boost the chances of offshore projects, which have lengthier development timelines than their onshore counterparts. The U.S. offshore wind industry remains in the nascent stage, but Deepwater Wind LLC's $225 million, 30-megawatt wind farm off the coast of Rhode Island last year became the first U.S. offshore wind farm to plant turbines in the water.

"There are not a lot of projects that are far enough advanced to be able to get there," said Keith Martin, who co-chairs Chadbourne & Parke LLP's project finance practice. "The handful of projects that are within reach will clearly be helped by this decision."

Bigger winners might be developers of geothermal, biomass and hydroelectric projects that have to start construction by year's end in order to qualify for the PTC, according to Jenner.

"All of those projects tend to be custom-made, the parts are built specifically for the project, and as a consequence, it takes longer," Jenner said. "This is welcome news."

But while the four-year safe harbor is a boon for new projects, it could make the future of older projects a bit dicier, experts say. For example, developers who started construction on wind projects in 2012 have only until the end of this year to complete them. If they don't, they'll have to demonstrate continuous work in order to qualify for the PTC, a tall order if a project is taking at least four years to complete.

"Developers who have been arguing that it took only minimal work to start construction under the physical work test may find that this comes back to haunt them," Martin said. "The biggest takeaway for lawyers is that the notice puts more pressure on how much physical work is enough for a project to be considered under construction."

But even if developers can't complete their projects within the four-year safe harbor, the IRS still appears willing to cut them a little slack. The new guidance also revises the list of "excusable disruptions" to a project, events outside the developer's control that could prevent a project's timely completion.

The existing list included things like weather delays or regulatory hurdles, but experts say a notable addition is delays related to interconnection — hooking the project up to the electric grid.

"Potential delays in interconnection to the grid have become a major concern for developers in planning to meet the continuity safe harbor," Jenner said. "By extending the continuity period to four years, and by providing that delays in interconnection are considered to be excusable disruptions, that gives developers considerable flexibility in meeting the continuity requirements."

It remains to be seen if the IRS takes a similar approach when it issues updated guidance for the investment tax credit for solar facilities, which was also extended in December. But it's safe to say the agency had one eye on the PTC's future when crafting the new guidance and extending the safe harbor, experts say.

The multiyear phaseout of the credit agreed to by Congress could indicate that there will be no future extensions. If that's the case, developers need specific direction from the IRS in order to take advantage of a closing window, and Jenner says the agency's new PTC guidance goes a long way to ensure as many viable projects as possible can claim a portion of the credit before it goes away.

"They've created a nice, soft landing strip," Jenner said.

--Editing by Katherine Rautenberg and Catherine Sum.