SEYFARTH SHAW LLP ATTORNEYS

One Minute Memo®

60s

Last Minute Extension and Modification Finally Comes for Renewable Energy Tax Credits

After many months of discussion and opposition, the American Taxpayer Relief Act of 2012 (the Act), signed into law by President Obama on January 2, 2013, to avert the fiscal cliff, extended and modified the laws surrounding renewable energy credits through January 1, 2014, some of which were set to expire December 31, 2012.

Specifically, under the Act, the availability of both the renewable electricity production tax credit (PTC) and the energy investment tax credit (ITC) have been extended for qualifying wind facilities that "start construction" before January 1, 2014. Under prior law, the tax credits were generally available for production from qualified wind facilities that were "placed in service" prior to the expiry date. The wind industry had expressed concern that the extension of the credit period alone would not be sufficient to encourage construction of new projects in 2013 because of the time it takes to place a qualifying facility in service, especially since many of the proposed projects from 2012 were either put on hold or scuttled. This change is intended to reduce uncertainty regarding the availability of the tax credits for project developers and encourage the construction of more projects in the coming year without fear of missing the deadline to take advantage of the tax credits. In addition to wind facilities, this new "start of construction" standard is also now applicable to a number of other renewable energy facilities, including closed-loop biomass facilities, open-loop biomass facilities, geothermal energy facilities, landfill gas facilities, trash facilities, qualified hydropower facilities, and marine and hydrokinetic energy facilities.

The Act does not define the term "start construction." For purposes of the cash grant that the Treasury Department has awarded under Section 1603 of the American Recovery and Reinvestment Act of 2009 (the "1603 Grant"), "begin construction" required that either "physical work of a significant nature" had begun or that at least 5% of the cost of the project had been paid or incurred. On the other hand, for purposes of a similar safe harbor in the Treasury regulations relating to "bonus depreciation," construction is not considered to begin before the taxpayer incurs or pays more than 10% of the cost of the project. The absence of specific guidance with respect to the PTC and ITC leaves some ambiguity as to whether and when the standard is met.

The PTC and ITC have had a long and complicated history. The PTC first appeared in the Internal Revenue Code in 1993. While it was initially scheduled to expire for facilities placed in service after June 30, 1999, it was repeatedly extended at the urging of the renewable energy industry. The PTC is a tax credit equal to a certain amount per kilowatt-hour of electricity produced by wind and other renewable energy sources that is sold to unrelated third parties. The amount of the credit per kWh is adjusted for inflation, so while it is currently equal to 2.2¢ per kWh, the amount of the credit should increase over time. The PTC is only available for the first ten years of the productive life of qualified renewable energy facility.

Starting in 2009, producers of wind and other renewable energy have been able to elect to take the ITC in lieu of the PTC. The ITC is a tax credit equal to 30% of capital expenditures for the construction of qualified wind and other renewable energy facilities. (The 1603 Grant in lieu of the ITC for facilities placed in service between 2009 and 2011 has not been extended since its expiration.) For both the ITC and the PTC, unused credits may be carried forward for twenty years.

The availability of both the PTC and the ITC has been crucial in financing wind and other renewable energy projects. Because most of these projects aren't initially profitable, it can be difficult to attract investors in the absence of these valuable tax credits. As the American Wind Energy Association notes, in years when the credits appear to be expiring, the number of new wind-energy projects drops dramatically.

In addition to the extension and modification relating to the ITC and PTC, the Act also extended the 50% "bonus depreciation" for qualified property, another important factor in obtaining financing for wind and other renewable energy projects. Bonus depreciation is now available for qualified property that is acquired and placed in service before January 1, 2014. For certain long-production-period property, bonus depreciation is now available for qualified property that is acquired before January 1, 2014, and placed in service before January 1, 2015.

The extension and modifications of the PTC and ITC under the Act represent hard-fought victories by the wind and other renewable energy industries. Due to these changes, as well as the Act's extension of bonus depreciation, we should expect to see a strong increase in new projects, and willing investors, over the coming year.

By: *Roy Meilman* and *Michael Rosenthal*

Partner, *Roy Meilman* and Associate, *Michael Rosenthal* are members of the corporate department in the firm's New York office. If you would like further information, please contact your Seyfarth attorney, or Roy Meilman at *rmeilman@seyfarth.com* or Michael Rosenthal at *mrosenthal@seyfarth.com*.

SEYFARTH ATTORNEYS SHAW LLP

www.seyfarth.com

Breadth. Depth. Results.