

## Client Alert

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# Notice 2014-46 Provides Additional Guidance on Eligibility of Wind and Other Renewable Energy Facilities for the PTC or the ITC

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On August 8, 2014, the Internal Revenue Service (IRS) released Notice 2014-46 (the "Notice"), which provides some important clarifications with respect to the requirement that construction of a project commence prior to January 1, 2014 for renewable energy facilities to be eligible to claim the production tax credit (PTC) and investment tax credit (ITC).

The IRS previously issued guidance (hereinafter, the "Prior Guidance") providing two alternative methods by which a taxpayer can demonstrate that construction on a renewable energy facility had begun before January 1, 2014, which is a prerequisite to claim the ITC or PTC for certain renewable energy facilities including wind, geothermal, biomass, landfill gas, incremental hydroelectric and ocean energy projects.<sup>1</sup> The first method requires a taxpayer to have begun physical work of a significant nature before January 1, 2014 (the "Physical Work Test"). The second method provides a safe harbor if at least 5% of the total cost of the facility was paid or incurred before January 1, 2014 (the "Safe Harbor").

The renewable energy industry has eagerly awaited additional guidance from the IRS, and should largely be satisfied with the guidance in the Notice, with respect to at least two areas of uncertainty in the Prior Guidance on the commencement of construction requirement. Specifically, some industry participants have questioned whether a minimum amount of work must be done or a minimum amount or percentage of money must be spent in connection with satisfying the Physical Work Test. Another area of uncertainty has been in what circumstances a facility or equipment that had satisfied the Physical Work Test or Safe Harbor retains that qualification after it has been transferred to a third party or a new site. In addition to addressing these two issues, the Notice provides a favorable modification to the Safe Harbor for certain facilities.

### PHYSICAL WORK TEST

Many investors were concerned that the Prior Guidance effectively required that a "significant" amount of physical work be performed for a facility to be eligible under the Physical Work Test. The Notice clarifies that there is no minimum amount of work or monetary threshold required to satisfy the Physical Work Test. Rather, the focus of the Physical Work Test is the nature of the work performed. The Notice reiterated examples provided in Notice 2013-29 that included excavating a foundation, pouring concrete for a foundation, installing anchor bolts, building integral roads and working on a custom-designed step-up transformer. Moreover, the Notice indicates that work of

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<sup>1</sup> Notice 2013-29 as clarified by Notice 2013-60. See our prior client alert on these Notices at <http://media.mofo.com/files/Uploads/Images/130926-Notice-2013-60.pdf>.

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the nature provided in the examples only need to have begun but does not need to have been completed before January 1, 2014.

## TRANSFERS OF FACILITIES

The Notice generally provides favorable guidance with respect to the transfer of ownership of a facility and relocation of equipment from one facility owned by a taxpayer to a different facility. Specifically, the Notice clarifies that a taxpayer may transfer a facility to a third party without jeopardizing the project's status as having commenced construction, emphasizing that the Internal Revenue Code and Prior Guidance "require only that construction of a facility begin before January 1, 2014. They do not require the construction to be begun by the taxpayer claiming the credit." Thus, if it satisfied the Physical Work Test or Safe Harbor with respect to the transferor, the facility generally would also satisfy the test for the transferee.

However, the Notice provides an exception for transfers consisting of solely tangible personal property to an unrelated transferee. Such transfers will not carry with them the "grandfathered" status and therefore a project using such personal property will not meet the requirement that construction commence prior to January 1, 2014 absent the project otherwise meeting the Physical Work Test or Safe Harbor. The intention of this restriction is to prevent taxpayers that had acquired renewable energy equipment with no intention of using that equipment from reselling the equipment to third parties at a premium (i.e. dealing in grandfathered equipment). If other contractual rights are transferred along with the tangible personal property, however, such transfers will be grandfathered.

In addition, the Notice clarifies that a taxpayer may relocate Safe Harbored equipment from one project site to another without generally jeopardizing the Safe Harbor status associated with that equipment.

## MODIFICATION OF SAFE HARBOR

The Notice modifies the Safe Harbor in the case of a single project comprised of multiple facilities in which a taxpayer paid or incurred less than 5%, but at least 3%, of the total cost of the facility before January 1, 2014. In that instance, a taxpayer may still meet the safe harbor so long as the cost of the included facilities does not exceed 20 times the amount that the taxpayer had incurred prior to January 1, 2014. Previously, a taxpayer could redefine a project to include fewer facilities only in situations where the Safe Harbor was not satisfied with respect to the larger project due to cost overruns.

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