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Shaines & McEachern, PA

RENEWABLE ENERGY GRANT GUIDELINES FINALLY ANNOUNCED

Preliminary Guidelines Announced Ahead of August Start-Date
Portsmouth, NH (July 12, 2009)

The US Department of Treasury has finally released guidelines for the cash grant program for renewable energy that has been part of February's American Recovery and Reinvestment Act stimulus bill but has never been implemented. (See "Payments for Specified Energy Property in Lieu of Tax Credits" at <http://www.treas.gov/recovery/1603.shtml>).

Like so much of the stimulus money targeted to improving the economy, the money stayed in Washington and has not been released. Billions of dollars targeted at renewable energy have languished in bureaucratic inactivity. According to inside sources at the DOE and US Treasury, they just didn't want to make the same mistake as the bank bailout from last fall when billions were handed out without much accountability. The funding delays have caused a growing discontent that without the stimulus bill's funding, projects would get cancelled and developers would lose focus and interest. The release of the preliminary guidelines this past Thursday will likely rekindle project initiatives, particular among solar PV developers.

A major feature of the \$3-billion set aside for green energy in February's stimulus bill was the transition of 30% tax credits to an outright 30% tax-free grant. (See "Where and How the New Stimulus Bill Begins Transforming the Nation's Energy," 24 March 2009; <http://www.greenenergylaw.org/Mondaq.pdf>). The tax credit and other tax features such as accelerated depreciation had been successful initiatives from previous legislation. But with so much of the investor landscape weakened by the economic downturn, few were willing to take risks in exchange for just tax credits - tax appetites disappeared as fast as investor money in 2008. No one wants credits that they cannot use.

Big Boost for Solar PV

For solar power developers in particular, this grant in lieu of credit filled a critical funding gap that made projects financially viable. Cash is always king, particularly in a recession, Uncle Sam had the answer with tax-free funding and solar developers in particular had real reason for excitement. (See <http://www.greenenergylaw.org/NEWS-Renewable-Energy-Industry-Needs-More.pdf>).

However, the Treasury Department isn't accepting grant applications yet. Last week's announcement were only preliminary guidelines which do not provide the full information on how to apply for the grants, only "to give ample time for businesses to prepare applications and expedite implementation of this program." The real applications and process will be posted around August 1st.

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Major Highlights

In brief, projects applicable under IRC §§ 45 and 48 that are placed into service after the start of this year through to the end of 2010 will be eligible for the grants. The Treasury claims it will issue funds within 60 days of receiving each application. The application process targets §1603 of the Recovery and Reinvestment Act. <http://www.greenenergylaw.org/ARRA.pdf>.

Solar property specifically qualifies under IRC §48. The funds are tax-free (not included in taxable income) and the basis of the property is reduced by ½ of the grant payment.

The major highlights include:

1) Generally, only “for profit” entities are eligible. Most foreign persons or entities, governments, not-profit IRC §501(c) entities and those using clean energy bonds under IRC §54 are not eligible. Non-business projects described in IRC §25C and residential energy efficient property under IRC §25D also are not eligible.

2) Tax credits under IRC §45 and §48 cannot be used or combined with these grants;

3) Applicant must be either the owner or lessee of the property; or if lessee, the lessor must provide waiver of receiving these grant funds (see comments below for possible sale-leaseback configurations).

4) The property must be depreciable or amortizable.

5) Project “placed in” service and construction dates are critical (see notes below).

6) Annual certifications and records and document maintenance by the project owner for 5 years including certifications that the property has not been sold or disposed of to a disqualified entity and that the project remains in compliance with the requirements of §1603. A transfer to a non-qualified owner will result in a “grant recapture” of as much as 100% of the funds which then must be returned to the government as a liability due the US Treasury enforced by the Department of Justice. This ‘recapture” will not apply as the rules now stand for projects that temporarily cease production as long as the project owner intends to resume production “at the time production ceases.”

7) Possible inspection by government inspectors of both the project and project documents to confirm compliance.

8) Payments made within 60-days from the later of the date of the complete application or the date the property is placed in service, after being “reviewed.”

9) Applications may only be submitted after the property has been placed in service or is under construction.

10) Application deadline (as it now exists) is October 1, 2011.

11) Each application entity must have a Data Universal Numbering System (DUNS) from Dunn & Bradstreet and must be registered with the Central Contractor registration (CCR) (see www.ccr.gov/startregistration.aspx).

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Placed in Service Dates and Deadlines

Qualified property must be either placed in service between the start of this year through to December 31, 2010 regardless when construction actually begins, or placed in service after 2010 as a “credit termination date” if construction is started before December 31, 2010. These “credit termination dates” vary by specified energy property ranging from “large wind” which must qualify by January 1, 2013, to geothermal heat pumps which have until January 1, 2017. Construction begins when “physical work of a significant nature begins” but does not include preliminary activities such as securing financing or project design work. A “safe harbor” for “significant” is where more than 5% of the total cost has been incurred. Contracts must not include a limit on damages of no more than 5% and must not include a full refund of a purchase price in lieu of any damages allowable by law in the event of a breach or cancellation.

Major Administrative and Legal Hurdles for Developers

As noted above, there are several key eligibility and compliance hurdles that could be missed without careful planning. The 5% safe harbor” threshold applies the economic performance standards of IRS §461(h). (See http://www.irs.gov/pub/irs-utl/construction_-_percentage_of_completion_timing_of_cost_recog.pdf). The beginning of construction will likely vary by type of project and its scale. Components of a project that are functionally interdependent will be considered a single component, the example used by the treasury is a wind turbine, tower and pad in which each is considered part of a “single unit of property” as compared to the control systems and arguably interconnecting power lines which are separate. But the owner may elect to treat the total project as a single unit for purposes of applying the timing safe harbor rules. In that case, failure to complete the entire project will not preclude receipt of the §1603 grant, but would limit the amount of the funding based upon what portion of the project is completed or “placed in service” by the deadlines. For solar projects such as roof-top panels in commercial settings, included in the calculation of the grant is the cost of the solar property and the cost of mounting and as well as power storage and conditioning equipment parts, but not the possible acquisition of the building or the transmission equipment such as transmission lines and towers that may be required. The details remain grounded and guided by qualified facilities definitions and regulations of IRC §§ 45 and 48, and §1.48(c) and (d) *et seq.*

Projects must be at least 80% new property used by the applicant; and may contain up to 20% used parts. Applicants must submit documentation demonstrating property is eligible, including final engineering design plans stamped by a licensed professional engineer as well as nameplate capacity. Specific regulations apply to small wind facilities under 100kW, closed and open-loop biomass electrical generation, geothermal facilities and hydropower including marine hydrokinetic power. In short, there is guidance for a wide variety of renewable energy projects.

Proof or documentation of the project costs includes copies of all contracts, copies of all invoices, proof of payment and an independent accountant’s certification for projects in excess of \$500,000

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Lessor-Lessee Leasebacks

One caveat of asset transfers is a three-month window in which a project may be placed in service, then sold to an applicant who then leases back the property. If this is accomplished, according to the preliminary guidelines, the applicant-lessor is considered the original user and the project is considered "placed in service" not earlier than when used under the lease-back arrangement. Applying this scheme, several deadlines may be inadvertently triggered or breached that could disqualify an otherwise qualified project, costing a project developer the 30% credit. However arranged, the lessee must be the entity that originally placed the project in service, the project must be sold and leased back to the same lessee within the 3-months after the "placed in service" date and both lessee and lessor must agree to not circumvent the sale-leaseback rules. Likewise, the an eligible lessor may elect to pass-through the grant money to a lessee, in which then this election treats the lessee as the owner in the same way as energy tax credits. The parties must agree that the lessor waives rights to the grants or other possible production or tax credits and the lessee must agree to include 50% of the grant as its income over the 5-year recapture period noted above.

Eligible Tax-Basis Calculations

The basis used to calculate the grant is generally the project's cost basis applying IRC §1012, unreduced by any other adjustment to that basis such as depreciation. Cost includes installation and shipping. Costs deducted for tax purposes such as IRC §179 deductions are not included in the cost basis calculations. Likewise, capitalized activities such as geothermal drilling that would not otherwise be depreciated or amortized cannot be calculated in the cost basis. (Note: treasury guide does include amortized deductions under IRC §59(e)).

DOE Issues Rules for \$3.9 Billion in Smart Grid Stimulus Grants

Related to the grants guidelines announcement was the issuance, also on Thursday, by the Department of Energy of the long-awaited guidelines for utility companies and grid infrastructure improvements. Full details on this at <http://www.greenenergylaw.org/DOE.pdf>.

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Wolf created the <http://www.GreenEnergyLaw.org> web-site to spearhead the law firm's renewable energy legal services. Since 1966, Shaines & McEachern has been a leading regional law firm engaged in the general practice of law with an emphasis on the region's small and medium-sized business clients. Attorneys at the firm are licensed to practice in New Hampshire, Maine, Massachusetts, U.S. District Courts, U.S. Court of Appeals, U.S. Military Court of Appeals, and the U.S. Supreme Court. Visit www.Shaines.com for more details. Offices located in Portsmouth, Boston and Kittery, Maine.

Contact: Rob Wolf @ 603-436-3111; rwolf@shaines.com or rob.wolf@greenenergylaw.org
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