

New Long-Term Extension of Wind and Solar Tax Credits Subject to Phase-out

Congress extends tax credits for wind and solar energy projects, but will phase the credits out over several years.

The Consolidated Appropriations Act, 2016 (the Act), which President Obama signed into law on December 18, 2015, re-enacts the production tax credit (PTC) and investment tax credit (ITC) for wind energy projects and modifies and extends the 30% ITC for solar energy projects. For both resources, the Act generally provides a five-year extension, with a step-down in the amount of credit available depending on when construction of a project commences. For solar energy projects, the Act modifies the eligibility rules from a “placed-in-service” requirement to a “begun-construction” requirement, similar to the existing rules for wind energy credits. Assuming the Internal Revenue Service (IRS) adopts guidance similar to the existing guidance for wind energy credits, the Act’s changes generally will allow developers at least seven years to complete new and existing projects.

Wind Energy Credits

Internal Revenue Code (Code) Section 45 allows taxpayers to claim PTCs for each kilowatt hour of electricity produced by a qualifying wind facility and sold to unrelated persons during a 10-year period following the facility’s placed-in-service date. Since 2009, taxpayers have had the option of electing to claim a 30% ITC in lieu of PTCs for qualifying wind facilities. Prior to the most recent expiration of the PTC, an owner of a qualifying wind facility could claim PTCs (or an ITC in lieu of PTCs) if construction of the facility began before January 1, 2015. Under IRS guidance, a taxpayer generally could establish the commencement of construction either by incurring 5% of the total eligible costs of the facility, or by commencing actual physical construction of the facility, prior to the deadline. Thereafter, the taxpayer is required to make “continuous efforts” or maintain a “continuous program of construction” to complete the facility. This continuity requirement is deemed satisfied if the facility is placed in service within two years of the deadline for commencing construction (*i.e.*, December 31, 2016).

The Act re-enacts and extends the PTC for wind facilities that begin construction before January 1, 2020, but steps down and phases out the amount of the credit over time, based on the construction start date. The Act also extends a taxpayer’s option to elect the ITC in lieu of PTCs for wind facilities, with an identical step-down and phase-out approach. The extension is retroactive to January 1, 2015, eliminating any eligibility gap for wind projects that commenced construction in 2015. Under the new rules, if construction begins:

- Before 2017, the facility is eligible for the full amount of PTCs or a 30% ITC
- During 2017, the amount of PTCs is reduced by 20% and the amount of ITC is 24%

- During 2018, the amount of PTCs is reduced by 40% and the amount of ITC is 18%
- During 2019, the amount of PTCs is reduced by 60% and the amount of ITC is 12%
- After 2019, the facility is not eligible for any PTCs or ITC

Solar Energy Credits

Code Section 48 currently allows taxpayers to claim a 30% ITC for solar energy facilities placed in service before January 1, 2017, and a 10% ITC for solar energy facilities placed in service on or after January 1, 2017. The Act generally supplants the “placed-in-service” requirement with a “begun-construction” requirement similar to that used for PTCs.

The Act extends the 30% ITC for solar projects that begin construction before 2020 and then provides for step-down in the amount of the credit to 10% over the next two years, with a hard placed-in-service deadline to claim any ITC greater than 10%. Under the new rules, if construction begins:

- Before 2020 and the facility is placed in service before January 1, 2024, the amount of ITC is 30%
- During 2020 and the facility is placed in service before January 1, 2024, the amount of ITC is 26%
- During 2021 and the facility is placed in service before January 1, 2024, the amount of ITC is 22%
- After 2021, the amount of ITC is 10%

Conclusion

The Act’s long-term extension of the federal tax credits for wind and solar energy projects should provide the necessary certainty and sufficient time for the development, financing and construction of significant additional generation capacity in the United States. While IRS guidance on the “begun-construction” requirement for wind energy credits will need to be updated and modified to address the Act’s changes, it is reasonable to expect that the new guidance will be similar to the existing guidance. Because the amount of credits is determined based on a project’s start construction date, developers will want to start construction as early as possible to take advantage of the biggest tax benefit and should maintain detailed documentation supporting the project’s start construction date.

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