FEDERAL INCENTIVES

Green Incentives and Credits for Businesses

RODMAN CPAs
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Investment Tax Credit Issues Summary

- Solar, Landfill Gas, Wind, Biomass, Hydroelectric, Geothermal Electric, Fuel Cells, Geothermal Heat Pumps, Municipal Solid Waste, CHP/Cogeneration, Hydrokinetic Power (i.e., Flowing Water), Anaerobic Digestion, Small Hydroelectric, Tidal Energy, Wave Energy, Ocean Thermal, Fuel Cells using Renewable Fuels, Microturbines,
- 30% tax credit on qualified basis
- 50% basis reduction in the property
- Accelerated five-year life
- Credit is offset to AMT- (could be a haircut)

Summary of ITC

- ITC of 30% extended to projects that begin construction by December 31, 2019
- Projects that start construction 2020 and 2021
  - Will receive 26% and 22% ITC respectively
  - All projects must be completed by 2024 to obtain elevated ITC rates
  - The new law provides a change from placed in service deadline to beginning construction deadline, which is considered a favorable modification for those claiming the credit

Business Energy Investment Tax Credit – Section 48

Summary

Note: The Consolidated Appropriations Act, signed in December 2015, included several amendments to this credit which apply to solar technologies and PTC-eligible technologies. Notably, the expiration date for these technologies was extended, with a gradual step down of the credits between 2019 and 2022.

The federal Business Energy Investment Tax Credit (ITC) has been amended a number of times, most recently in December 2015. The table below shows the value of the investment tax credit for each technology by year. The expiration date for solar technologies and wind is based on when construction begins. For all other technologies, the expiration date is based on when the system is placed in service (fully installed and being used for its intended purpose).

Technology	12/31/16	12/31/17	12/31/18	12/31/19	12/31/20	12/31/21	12/31/22	Future Years
PV, Solar Water Heating, Solar Space Heating/Cooling, Solar Process Heat	30%	30%	30%	30%	26%	22%	10%	10%
Hybrid Solar Lighting, Fuel Cells, Small Wind	30%	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Geothermal Heat Pumps, Microtubines, Combine Heat and Power Systems	10%	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Geothermal Electric	10%	10%	10%	10%	10%	10%	10%	10%
Large Wind	30%	24%	18%	12%	N/A	N/A	N/A	N/A

Chart from dsireusa.org

Passive vs. Active

- Passive issues (Unless have Passive Income)
  - Must materially participate to be active (for individuals)
    - Treasury has rules/test
      - *C Corps does not apply*
      - *Grouping can be an option*
  - Limits losses and credits through Passive Activity Loss (PAL)
    - PAL can be offset against other Passive Income
    - Losses can be carried forward
    - Credits can be carried forward (carried back 1 year, carried forward 20 years) – Must carryback.

Passive Test

1. The taxpayer participates in the activity for more than 500 hours during the year,
2. The taxpayer’s participation in the activity constitutes substantially all of the participation by all individuals (including non-owners) in the activity for the year,
3. The taxpayers’ participation is more than 100 hours during the year, and no other individual (including non-owners) participates more hours than the taxpayer,
4. The activity is a significant participation activity in which the taxpayer participates for more than 100 hours during the year and the taxpayer’s annual participation in all significant participation activities is more than 500 hours,
5. The taxpayer materially participated in the activity for any five years (whether or not consecutive) during the 10 immediately preceding tax years,
6. For a personal service activity, the taxpayer materially participated for any three tax years (whether or not consecutive) preceding the current tax year, or
7. Based on all the facts and circumstances, the taxpayer participates on regular, continuous, and substantial basis during the year.

Depreciation

- Bonus Depreciation expires 2017 (50%), phases out 40% in 2018, 30% in 2019
- Example depreciated over 5 year life under accelerated depreciation
- Accelerated Depreciation

Cost	**100,000.00**
Year 1 Depreciation	20,000.00
Year 2 Depreciation	32,000.00
Year 3 Depreciation	19,200.00
Year 4 Depreciation	11,520.00
Year 5 Depreciation	11,520.00
Year 6 Depreciation	5,760.00

In Service Test

Here are the 5 criteria that we have used in the past with other projects

1. The Project must have obtained the necessary permits and licenses for operation.
2. The Project must have completed all critical pre-operational testing.
3. The Owner must have has taken control of the facility. [*In order to satisfy this criteria the Owner must demonstrate that it has care, custody, and control and that title and risk of loss has passed to the Owner.]*
4. The energy property has been synchronized with the transmission grid.
5. The energy property has begun daily or regular operation.

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Structuring Options

for

ITC Monetization

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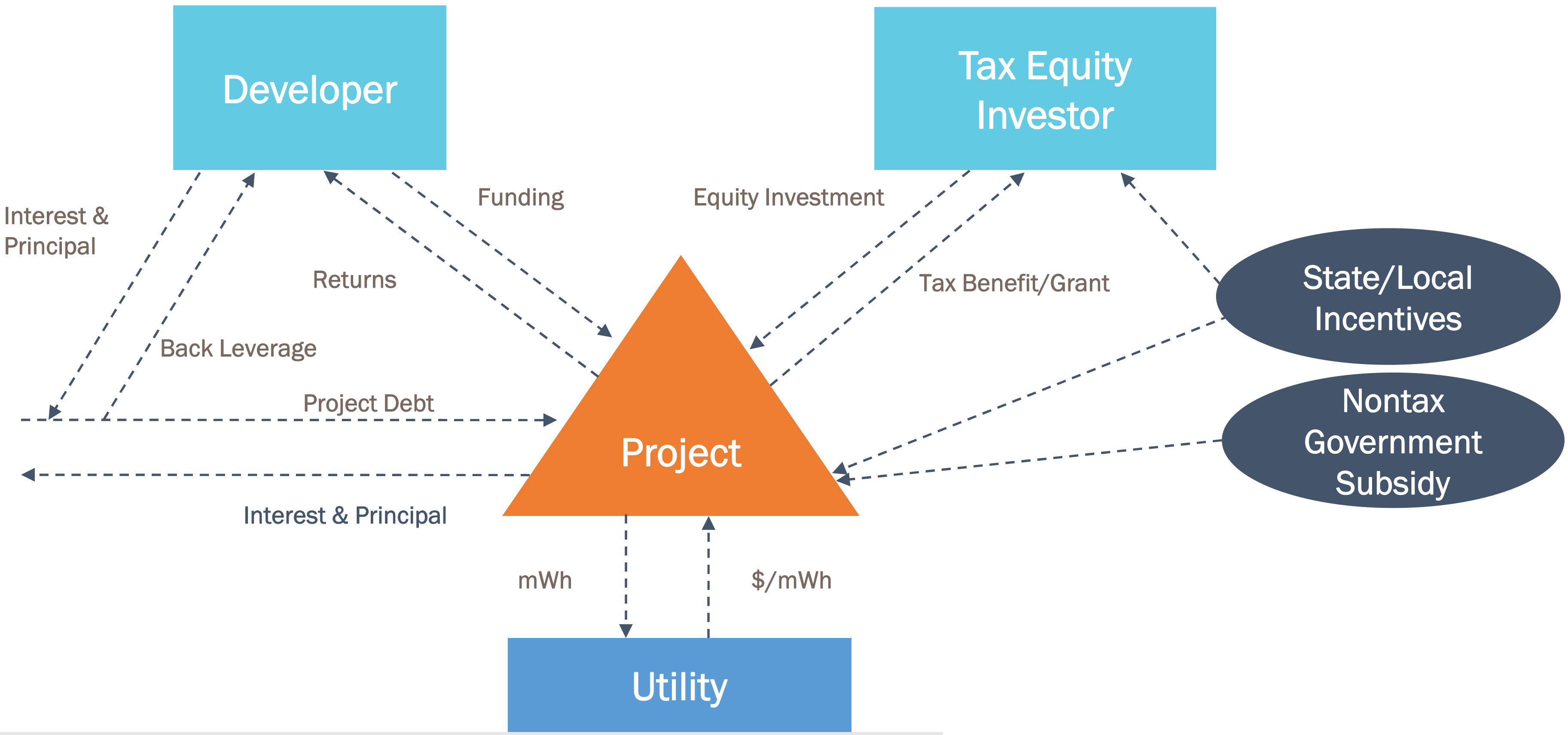
Tax Equity

- Limitation on credit for those who have losses
- Hard to find
- Some deals are "too small"
- Passive issues
- At Risk Rules
    - Recourse debt (at least 80%)
- Tax Structure
    - Partnership flip
    - Sale – lease back
    - Inverted lease
    - Consider bundling projects

Equity Flip Partnership (PTC & ITC)



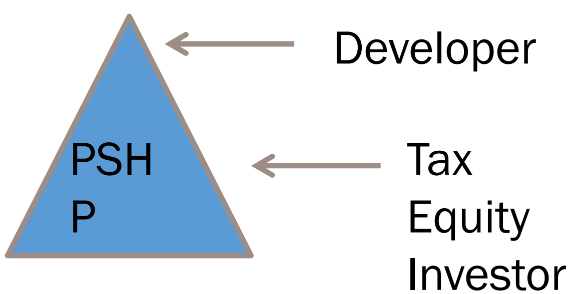
This structure provides the tax investor with special allocations of the credits and depreciation in order to provide a return on their investment, although they will bear some amount of operations risk during the early years, while the developer is able to monetize the tax benefits that could not be utilized and bears the operating risk throughout the investment.

Note: Federal income tax rules must be followed for the structure and allocations to be respected; this structure may not work for tax-exempt investors.

Equity Flip Partnership (Cont.)

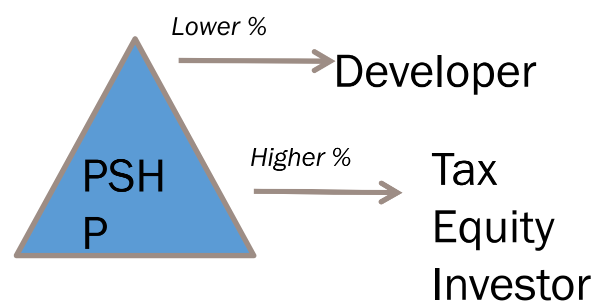
FORMATION:

- The Tax Equity Investor's contribution is derived based on anticipated return:
  - Cash
  - Tax Credits
  - SALT Incentives
  - Depreciation Deductions

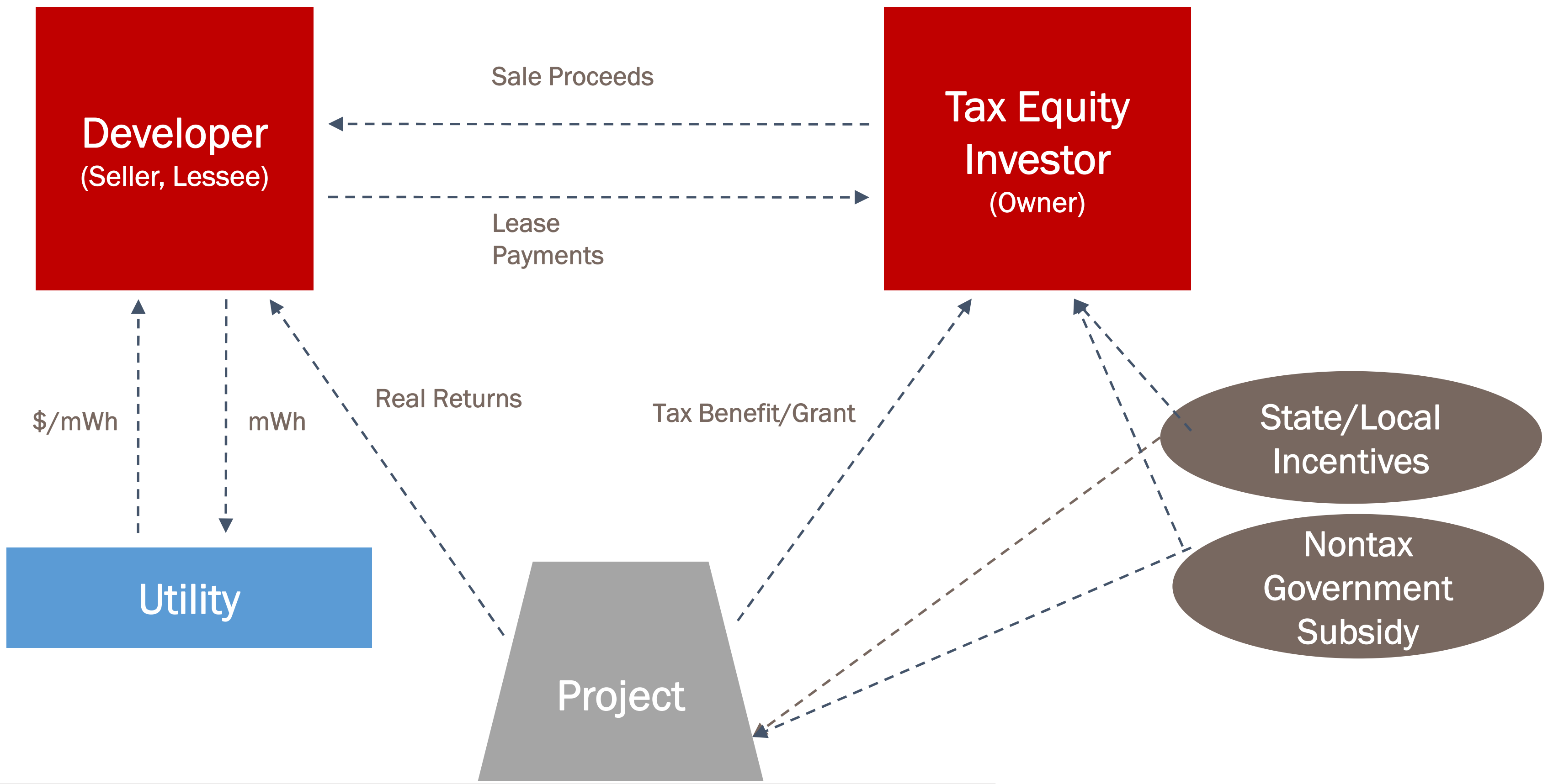


YEAR 1:

- Tax Equity Investor receives a substantial percentage of:
  - Cash
  - Tax Credits
  - SALT Incentives
  - Depreciation Deductions



Sale Leaseback (ITC Only)



In this structure, the tax investor is the owner/lessor and, as such, is entitled to the credits and depreciation. The tax investor further benefits by being able to mitigate operations risk through locking in purchase price and stream of rental payments. The developer is able to receive up-front proceeds from the sale of property, while transferring full ownership of the property. This transaction must occur within 90 days of the original placed-in-service date.

Note: A PPA should be examined for sale of electricity to a third party to mitigate potential price shifts.

**Recapture potential of credit if developer buys back the property in a certain time period.*

Sale Leaseback (Cont.)

- The developer sells eligible equipment to Tax Equity Investor at retail.
- Tax Equity Investor subsequently leases back to developer
- Tax Equity Investor benefits by reaping tax credits, SALT incentives, depreciation deductions, and payments
- Tax Equity Investor:
  1. Responsible for all capital infusion
  2. Calculates lease payments to achieve return

- ➢ Developer: responsible for maintenance on equipment
- ➢ Developer sells energy to utility
- ➢ Payments are mandatory regardless of profitability or revenue streams
- ➢ Buy out option usually exists at conclusion of lease

Summary of Two Investment Options

- Choice of transaction depends on Investor’s capital, liquidity, need for return:
  1. The “flip” affords investor more flexibility
  2. Leaseback does not require substantial initial capital infusion

<u>Leaseback</u>:
- If the equipment operates effectively early, “flip” occurs earlier.
- If equipment performance is lacking, “flip” is delayed.

<u>“Flip”</u>:
- If the equipment operates effectively early, more revenue is generated.
- If it under performs, less revenue materializes.

Either way the lease payments are constant and for a defined term.

State Tax Incentives

http://www.dsireusa.org/
(Database of State Incentives for Renewable Energy)

What do Investors Seek

What do investors seek?

- What is the initial investment that the business require?
- How much control will you have vs. investor?
- When will the business turn a profit?
- When can investor get back their money?
- What is the return on investment?
- Are you fully committed to the business?
- What are the profit distributions?
- What if the company fails, do you have a backup plan?
- Is there a tax appetite?

Steps to take: STEP ONE

- Present a **<u>business</u>** not just an idea
  - Have a business plan (*does not have to be long)*
    - Executive summary
    - Opportunity
    - Market analysis
    - Execution
    - Company and management summary
    - Financial Plan

Steps to take: STEP TWO

- Cash flow projection
  - Review numbers and cash flow
    - Does it make sense?
    - Has an accountant reviewed?
    - Assumptions correct and listed out?
    - Easy to read and understand.
    - How realistic is it?

Steps to take: STEP THREE

- Resources
  - What resources do you have?
    - Capital resources
    - Talent
    - Equipment
    - Who are your players?

Steps to take: STEP FOUR

- Research the Investor
  - Who is your target investor?
    - Do due diligence.
    - Do you have a connection?
    - What can you learn?

Steps to take: STEP FIVE

- Strategy
    - What is your vision and strategy?
        - How will you grow?
        - What is the exit strategy?
        - What are your barriers?
            - How will you overcome them?
        - What is your timeline?
        - Why would the investor want to choose you?

THANK YOU

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