



## STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA  
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082  
916-323-9856 • FAX 916-323-3387  
[www.boe.ca.gov](http://www.boe.ca.gov)

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February 20, 2014

**Re: *Active Solar Energy System New Construction Exclusion  
Assignment No.: 13-258***

Dear Mr. \_\_\_\_\_ :

This is in response to your request for a legal opinion regarding whether the sale of 100 percent of the membership interests in a limited liability company (LLC) or other special purpose entity owning a newly constructed solar energy system disqualifies the solar energy system from eligibility for the new construction exclusion under Revenue and Taxation Code<sup>1</sup> section 73. As explained below, it is our opinion that the purchaser of interests in a legal entity owning a newly constructed active solar energy system can claim the active solar energy new construction exclusion, provided that another taxpayer has not received the exclusion for the same solar energy system.

### **Factual Background**

According to your letter, \_\_\_\_\_, Inc. (Company) is a major developer and seller of photovoltaic energy solutions, and provides design, installation, financing, monitoring, operations, and maintenance services to the solar market to provide a comprehensive solar energy service to customers. In 2011, Company relocated its headquarters for its solar energy business to California.

Company offers roof-mounted systems, parking canopy systems, and fixed or tracking ground-mount systems. Company's solar energy customers fall into three categories: (1) commercial customers, principally including large, national retail chains and real estate property management firms; (2) federal, state and municipal governments; and (3) utilities. As of December 31, 2012, Company has interconnected over xxx solar power systems representing xxx megawatts (MW) of solar energy generating capacity, and has xx MW of projects under construction and another xx gigawatts of projects under contract for future construction.

Company develops and sells photovoltaic energy solutions to customers generally using one of two arrangements: (1) a sale-leaseback transaction; or (2) sale of interest(s) in a special purpose entity. In a sale-leaseback transaction, the parties enter into a long-term power purchase

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<sup>1</sup> All further statutory references are to the Revenue and Taxation Code unless otherwise specified.

agreement where customers purchase electricity at a pre-determined price for a period of time, which may be up to 20 or 25 years. The sale-leaseback transaction is not at issue in this letter.

The second arrangement, involving the sale of interests in a special purpose entity, is the subject of your inquiry. In such arrangement, Company constructs and sells completed solar energy systems to customers, transferring ownership and control of the system to the customer. Company does not retain any control or maintain the system. Prior to the sale of the system, the scope of work for the customer includes the complete design, engineering, procurement and installation for all equipment required for the project and complete construction of the solar energy system. Company effectuates such sales of the solar energy systems through the sale of Company's interest in a special purpose entity, typically a newly formed LLC, which owns the solar energy system at the completion of construction, so as to provide the purchasers federal tax benefits. In this arrangement, the active solar energy system has not received the benefit of the new construction exclusion under section 73 prior to the sale by Sun Edison to the LLC, and the transfer takes place within the three month, sale-leaseback "safe harbor" period. Based on your letter and for purposes of this analysis, we assume that 100 percent of the interests in the special purpose entities are being transferred.<sup>2</sup> Company's inquiry is whether the above-described sale of interests in a special purpose entity would disqualify the solar energy system from the exclusion from assessment under section 73, provided the sale of the interest in the special purpose entity takes place within a three-month period.

### **Law and Analysis**

California Constitution article XIII A, section 2, subdivision (a) provides in relevant part that full cash value of real property means the appraised value of real property as shown on the 1975-76 tax bill or "the appraised value of real property when purchased, newly constructed or a change in ownership has occurred after the 1975 assessment." Section 70, subdivision (a) defines "new construction", in part, as "[a]ny addition to real property, whether land or improvements (including fixtures), since the last lien date. . . ." Section 71 requires the assessor to determine the added value for newly constructed property upon completion.

In 1980, voters of Proposition 7 approved an amendment to the California Constitution to read that the term "newly constructed" excludes "the construction or addition of any active solar energy system." (Cal. Const., art. XIII A, subd. (c)(1).) Section 73, enacted to implement article XIII A, subdivision (c)(1) of the California Constitution, provides that the term "newly constructed" shall not include the construction or addition of any active solar energy system. The active solar energy system new construction exclusion remains in effect until a subsequent change in ownership occurs. (Rev. & Tax. Code, § 73, subd. (f).)

Section 73 was amended in 2008<sup>3</sup> to add subdivision (e), which allows the first buyer of a new building incorporating an active solar energy system to utilize the active solar energy system new construction exclusion, provided the owner-builder does not intend to occupy or use the building, the owner-builder has not received the active solar energy system new construction exclusion, the first buyer purchases the building prior to it becoming subject to reassessment to

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<sup>2</sup> We note, however, that a sale of less than 100 percent of the LLC would not change our opinion. Of course, if no change in control occurred as a result of the sale of membership interests in the LLC, no change in ownership of the real property held by the LLC would occur, and therefore, any use of the active solar energy system new construction exclusion would continue until a change in ownership of the property occurs.

<sup>3</sup> Stats. 2008, ch. 538 (Assembly Bill 1451).

the owner-builder pursuant to section 75.12 subdivision (d), and the first buyer files the appropriate claim form with the assessor.

In 2011,<sup>4</sup> the Legislature added intent language to section 73, to clarify that it was enacted to encourage the building of active solar energy systems, and that solar energy systems that are constructed as freestanding or parking lot canopies, or as installations on existing buildings, qualify for the exclusion. In the amendment to section 73, the Legislature recognized that newly constructed active solar systems are often sold or transferred in sale-leaseback arrangements, partnership flip structures, or other transactions to purchasers that may also be eligible for federal tax benefits.<sup>5</sup> As long as another taxpayer has not received an exclusion for the same active solar energy system, the Legislature declared that its intent is for the purchaser of the active solar energy system in such transactions to receive the active solar energy system new construction exclusion.

Under federal law, an owner-builder is given three months from the time the solar energy system is placed in service to enter a sale-leaseback financing arrangement and still receive the federal tax benefits.<sup>6</sup> Consistent with the Legislature's declared intent in AB X1 15 and aligning with federal law, the Board of Equalization has stated that parties to such financial arrangements should be allowed a three-month window for the transfer of a completed active solar energy system to allow the owner-builder to arrange for and execute the transaction post-construction. (*Guidelines for Active Solar Energy Systems New Construction Exclusion* (Letter to Assessors No. 2012/053 (December 6, 2012)) (*Guidelines*), at p. 8.)

Active solar energy systems owned by a legal entity, such as an LLC, are also excluded from the definition of new construction and are excluded from assessment. (*Guidelines*, at p. 11.) Generally, transfers or purchases of interests in legal entities do not constitute changes in ownership of the real property owned by those legal entities. There are two exceptions to this rule. First, when a change in control of the legal entity occurs, all real property in the entity is subject to reassessment. (Rev. & Tax. Code section 64, subd. (c)(1).) Second, when a legal entity's original co-owners cumulatively transfer more than 50 percent of their interest in a legal entity, real property previously excluded from change in ownership under section 62, subdivision (a)(2), will be reassessed.

Here, Company constructs and sells completed solar energy systems to customers through the sale of its interests in a special purpose entity, typically an LLC, which owns the solar energy system upon completion of construction. Before the sale to the purchaser, the LLC is owned 100 percent by Company. At some point after the completion of construction, Company transfers 100 percent of the ownership interests in the LLC to the purchaser. This causes a reassessment of all property owned by the LLC pursuant to section 64, subdivision (c)(1). However, the Legislature has declared that purchasers of a solar energy system may still receive the new construction exclusion even if the solar energy systems are transferred in "sale-leaseback arrangements, partnership flip structures, or other transactions to purchasers", as long as the active solar energy system is newly constructed or added and another taxpayer has not

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<sup>4</sup> Stats. 2011, ch. 3 (Assembly Bill 15 of the First Extraordinary Session [AB X1 15]), in effect June 28, 2011.)

<sup>5</sup> Rev. & Tax Com., Analysis of Assem. Bill No. AB 15 X1 (2011 1st Ex. Sess.) as amended June 2, 2011, p.2.

<sup>6</sup> See Internal Revenue Code (IRC) § 50(d)(4), making applicable the provisions of paragraphs (2) and (3) of IRC § 48(b) in effect the day before enactment of the Revenue Reconciliation Act of 1990 (relating to certain leased property).

received an exclusion for the same active solar energy system.<sup>7</sup> Therefore, it is our opinion that where 100 percent of the interests in an LLC owning a newly constructed solar energy system are transferred to a purchaser, the solar energy system may be excluded from reassessment as long as no other taxpayer has received an exclusion for the same active solar energy system. As explained in the *Guidelines*, the transfer to the purchaser should be completed within three months of the completion of construction of the solar energy system. (*Guidelines*, at p. 8.) In this case, your letter indicates that the active solar energy system will not have been excluded from reassessment under section 73 prior to the proposed sale and the sale was made within the federal three-month, sale-leaseback "safe harbor" period in order to provide the buyer the federal tax benefits. Therefore, the buyer of the entity which owns the completed solar energy system is eligible to claim the exclusion.

The views expressed in this letter are only advisory in nature; they represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,

/s/ Leslie Ang

Leslie Ang  
Tax Counsel

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cc: Honorable Larry W. Ward  
President of California Assessors' Association  
Riverside County Assessor

Mr. David Gau      MIC:63  
Mr. Dean Kinnee    MIC:64  
Mr. Todd Gilman    MIC:70

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<sup>7</sup> Rev. & Tax Com., Analysis of Assem. Bill No. AB 15 X1, *supra*, at p.1.