

Thank you for the chance to provide input on the BOE's "GUIDELINES FOR ACTIVE SOLAR ENERGY SYSTEMS NEW CONSTRUCTION EXCLUSION" document (the "GUIDE"). The meeting last Thursday was very informative. As promised, below is a description of the Federal tax benefits for which solar is eligible (other than the §48 Investment Tax Credit discussed in the meeting).

Similar to California's "new construction exclusion" that overrides the "change in ownership" tax trigger for solar energy system assessments, an analogous exclusion exists on the federal level that uses different criteria for triggering "change of ownership" tax consequences. It is extremely difficult for business to deal with conflicting tax consequences at the federal and state level. ABx15 1 was intended to fix this situation for solar systems sold or transferred in sale-leaseback arrangements, partnership flip structures, or other transactions reliant on federal tax preferences.

This note will explain the federal tax benefits offered to spur solar development, and their associated tax consequence triggering mechanisms. It will point out where the current BOE draft doesn't harmonize with tax triggers in the federal code.

FEDERAL TAX INCENTIVES FOR SOLAR:

In addition to the § 48 Investment Tax Credit available for solar in the US tax code, of which you are aware, there are also the following incentives:

- **5-Year Bonus Depreciation**

The 5-year schedule for most types of solar has been in place since 1986. See the US tax code: §168(e)(3)(B)(vi)(1). (See: http://www.law.cornell.edu/uscode/html/uscode26/usc_sec_26_00000168----000-.html)

The federal *Economic Stimulus Act of 2008*, enacted in February 2008, included a 50% first-year bonus depreciation provision for eligible renewable-energy systems acquired and placed in service in 2008. This provision was extended (retroactively for the entire 2009 tax year) under the same terms by *The American Recovery and Reinvestment Act of 2009*, enacted in February 2009. Bonus depreciation was renewed again in September 2010 (retroactively for the entire 2010 tax year) by the *Small Business Jobs Act of 2010 (H.R. 5297)*.

In December 2010 the provision for bonus depreciation was amended and extended yet again by *The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (H.R. 4853)*. For 2012, bonus depreciation is still available, but the allowable deduction reverts from 100% to 50% of the eligible basis.

- **Section 1603 Treasury Grant in lieu of the § 48(a)(3)(A) Investment Tax Credit (the "1603 Treasury Grant")**

Section 1603 of *The American Recovery and Reinvestment Act of 2009* was enacted in February 2009. Under that program, the United States Department of Treasury makes payments to eligible persons who place in service specified renewable-energy systems. By receiving payments for property under section 1603, applicants forego tax credits under § 48 and § 45 of the US tax code with respect to such property for the taxable year in which the payment is made, or any subsequent taxable year. The Section 1603 program was renewed again by Section 707 of *The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (Public Law 111-312)*.

The 1603 Treasury Grant Program modifies the "change of ownership" tax trigger dates for owners of solar energy systems on a federal level, similar to the way that Section 73 modifies such dates in California. Below is a description on how the "change of ownership" tax trigger dates differ before/after the recent federal legislation:

- § 48 Investment Tax Credit: If a solar property owners claims the § 48(a)(3)(A) Investment Tax Credit, and there is a change of ownership, or if the property ceases to qualify as a specified energy property within five years from the date the property is placed in service, then the Investment Tax Credit is revoked. Tax must be paid or

repaid to the Treasury according to a predefined formula. The elimination of this tax exemption upon “change of ownership” is called “recapture.” For solar projects financed via the § 48 ITC, the “change of ownership” definitions in the California Assessors’ Handbook are in harmony with the tax code.

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- The 1603 Treasury Grant: If a solar property owner claims the 1603 Treasury Grant instead of the § 48 ITC, there is a special exemption from the typical “change of ownership” tax definitions. More specifically, solar systems financed with the 1603 Treasury grant can be sold or transferred to any third-party who themselves would have been eligible for the 1603 Treasury Grant. Similar to Section 73 in California, this deviation from traditional ITC tax treatment was architected into the tax code to spur solar investment for the greater good. For solar projects financed via the 1603 Treasury Grant, the “change of ownership” definitions in the California Assessors’ Handbook are **NOT** in harmony with the tax code

Below are the direct quotes regarding the “change of ownership” definitions for projects financed with the 1603 Treasury Grant:

“Selling or otherwise disposing of the property to an entity other than a disqualified person does not result in recapture provided the property continues to qualify as a specified energy property and provided the purchaser of the property agrees to be jointly liable with the applicant for any recapture. Recapture would occur in the event the property is resold to a disqualified person or ceases to qualify as a specified energy property.” (see: <http://www.treasury.gov/initiatives/recovery/Documents/B%20Guidance%203-29-11%20revised%20%282%29%20clean.pdf>, Lines 10-16, Page 20)

To receive the 1603 Treasury Grant:

“Qualified property must be originally placed in service between January 1, 2009, and December 31, 2011, (regardless of when construction begins) or placed in service after 2011 and before the credit termination date [e.g., January 1, 2017]...if construction of the property begins between January 1, 2009, and December 31, 2011.” (see: <http://www.treasury.gov/initiatives/recovery/Documents/B%20Guidance%203-29-11%20revised%20%282%29%20clean.pdf>, Lines 13-38, Page 5).

Also, according to US Treasury, a transfer to a “disqualified person” (eliminating tax preferences) is defined as follows:

“Property is considered to have been disposed of to a disqualified person if any interest in the property or in the applicant or in any partnership or pass-thru entity that is a direct or indirect owner of an interest in the applicant is sold to: any Federal, state or local government, including any political subdivision, agency or instrumentality thereof; any organization that is described in section 501(c) of the IRC and is exempt from tax under section 501(a) of the IRC; any entity referred to in paragraph (4) of section 54(j) of the IRC; or any partnership or other pass-thru entity any partner (or other holder of an equity or profits interest) of which is a Federal, state or local government, including any political subdivision, agency or instrumentality thereof; an organization that is described in section 501(c) of the IRC and is exempt from tax under section 501(a) of the IRC; or an entity referred to in paragraph (4) of section 54(j) of the IRC. A taxable corporation some or all of whose shareholders are disqualified persons is not a disqualified person and such a corporation’s ownership of an interest in a partnership or other pass-thru entity will not cause the partnership or other entity to be treated as a disqualified person.” (see: <http://www.treasury.gov/initiatives/recovery/Documents/B%20Guidance%203-29-11%20revised%20%282%29%20clean.pdf>, Lines 14-27, Page 19)

The BOE codifies the interpretation of the tax code in the California Assessors' Handbook.

- As per the California Assessors' Handbook section 201, "The values appearing on the roll are set as of the date of change in ownership or completion of new construction..." (see: <http://www.boe.ca.gov/proptaxes/pdf/ah201.pdf>, Chapter 1, Lines 29-30, Page 2).
- Furthermore, the California Assessors' Handbook Section 501 defines "New Construction" as "Any addition to real property, whether land or improvements (including fixtures) since the last lien date; any alteration of land or improvements (including fixtures) since the last lien date that constitutes a major rehabilitation thereof or which converts the property to a different use." (see: <http://www.boe.ca.gov/proptaxes/pdf/ah501.pdf>, Glossary of Terms, Lines 40-43, Page 150).
- And the California Assessors' Handbook Section 401 defines "change of ownership" (for a legal entity, including one that owns a solar system) by referring to California Revenue and Taxation Code Section 64 which states: "When a corporation, partnership, limited liability company, other legal entity, or any other person obtains control through direct or indirect ownership or control of more than 50 percent of the voting stock of any corporation, or obtains a majority ownership interest in any partnership, limited liability company, or other legal entity through the purchase or transfer of corporate stock, partnership, or limited liability company interest, or ownership interests in other legal entities, including any purchase or transfer of 50 percent or less of the ownership interest through which control or a majority ownership interest is obtained, the purchase or transfer of that stock or other interest shall be a change of ownership of the real property owned by the corporation, partnership, limited liability company, or other legal entity in which the controlling interest is obtained."

Section 73 provides an exclusion that delays the assessment date (which would otherwise be defined in Chapter 1, Page 2, Lines 29-30, of the Assessors' Handbook section 201) for Active Solar Energy Systems. **ABx15 1 clarifies that the "new construction exclusion" in California Revenue and Taxation Code Section 73 should apply to** "newly constructed active solar energy systems [that] are often sold or transferred in sale-leaseback arrangements, partnership flip structures, or **other transactions to purchasers...eligible for federal tax benefits.**" When the federal tax benefits are utilized, then ABx15 1 clarifies the legislative intent that Section 73 should take precedence over the current assessment guidelines in the California Assessors' Handbook.

RECOMMENDATION:

On a Federal level:

1. If over 50% of the ownership or control of an entity owning a solar system is transferred, then this triggers "change of ownership" tax treatment—unless the solar system was financed with the 1603 Treasury Grant where special "change of ownership" rules below apply:
 - a. When the federal government passed Section 1603 of *The American Recovery and Reinvestment Act of 2009*, similar to when California passed ABx15 1, the legislature enacted an exemption to the "change of ownership" rules to support active solar energy systems sold or transferred in sale-leaseback arrangements, partnership flip structures, or other transactions. This "change of ownership" exemption specifically supports an active secondary market to finance these transactions.
 - b. Moreover, to further support these secondary market "other transactions"; so long as the new owner is not a "disqualified person," the secondary market owner of the solar system is themselves granted a new 5-Year bonus depreciation based on the new owner's basis in the system.

These Federal tax benefits, in force for active solar energy systems until October 1, 2017, support a securitization transaction where 50% or more of the ownership or control of a legal entity (owning an active solar energy system) is transferred to another eligible party. The Federal law and guidelines are an exemption crafted to override the normal date when Federal tax benefits would expire, and to override any potential “recapture” of previously granted tax benefits.

The most recent amendment to section 73 was chaptered June 28, 2011. It added legislative intent language declaring that section 73 was enacted to encourage the building of active solar energy systems. Without this recent amendment, it would not be clear if Section 73 should take precedence over the California Assessors' Handbook Section 401 regarding “change of ownership” treatment. However, ABx15 1 was specifically passed to clarify that, **in the case of transactions to purchasers eligible for federal tax benefits, Section 73 should take precedence over other areas in the California code when there is a lack of clarity or conflict** (as is the case in the “change of ownership” rules quoted in the California Assessors' Handbook Section 401).

To interpret Section 73, in light of this new legislation, the BOE has crafted the “GUIDE.” In all other areas covered in the “GUIDE”, the CA BOE assures consistency with federal tax triggers for benefits related to active solar energy systems. In keeping with this goal to provide a consistency, we respectfully submit that the **BOE would be inconsistent with Section 73, and inconsistent with treatment of other assessment criteria in the “GUIDE,” unless it harmonizes its “change of ownership” rules with those in place at the federal level.** As such, active solar energy systems financed with the 1603 Treasury Grant between January 1, 2009 and January 1, 2017 should be eligible for the “new construction exclusion” unless ownership transfers to a new person not eligible for the Federal tax benefits described herein.

Thank you again for the opportunity to provide feedback on the “GUIDE” document.

Best Regards,

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