



Corporate Tax Department
350 West Washington Street, Suite 600
Tempe, AZ 85281

November 22, 2011

Mr. Michael McDade
State Board of Equalization
Property and Special Taxes Department
PO Box 942879
SACRAMENTO, CA 94279-0064

RE: *Guidelines for Active Solar Energy Systems New Construction Exclusion*
Request for Comments and Revisions

Dear Mr. McDade:

On October 13, 2011 the Board staff issued a draft of the proposed *Guidelines for Active Solar Energy Systems New Construction Exclusion* under Section 73¹, and invited comments and any suggested revisions to the *Guidelines* on or before November 23, 2011.

We congratulate the Board staff on the issuance of these proposed regulations. We feel they are generally helpful in terms of explaining the rules and encouraging uniform application of the Section 73 property tax exemption for an Active Solar Energy System (*System*). However, there are certain aspects of the proposed *Guidelines* that we feel are in need of, and warrant, additional guidance and clarification in order to optimize the usefulness of these regulations, particularly in the case of larger commercial and Industrial Systems.

Accordingly, First Solar is pleased to submit comments for your review and consideration. First Solar believes these suggestions are necessary to further clarify the application of the Section 73 exclusion consistent with its legislative intent.

DEFINITIONS – ACTIVE SOLAR ENERGY SYSTEM:

The *Guidelines* describe an active solar energy system based on the language of Section 73 to include “storage devices, power conditioning equipment, transfer equipment, and parts related to the functioning of those items,” and further provide that such a system includes “only equipment used up to, but not including, the stage of transmission or use of the electricity.” In this regard one of the critical issues in a commercial *System* is determining where the *System* ends and where the stage of transmission begins. In this regard it would be very helpful for the *Guidance*

¹ All statutory references are to the Revenue and Taxation Code unless otherwise specified

to address this issue, rather than to leave the issue up to each assessor to decide for him or herself.

The answer to this issue can be found in the federal definition of *solar energy property*, which is subject to the 30% federal investment tax credit under Internal Revenue Code² (“Code) §48 or in the alternative the 30% federal grant under ARRA³ §1603. The federal definition of solar energy property is virtually identical to the California definition of active solar energy system⁴. For example, under the federal definition, solar energy property “includes storage devices, power conditioning equipment, transfer equipment, and parts related to the functioning of those items.”⁵ Also, virtually identical to the California definition, solar energy property includes “only equipment up to (but not including) the stage that transmits or uses electricity.” Thus, for federal purposes, the issue of where the solar energy property ends and where the transmission property begins is a critical issue, just as it is in the case of the Section 73 exclusion.

US Treasury made great strides in resolving the issue of where generation ends and where transmission begins earlier in 2011 when they released a general counsel memorandum considering this very issue. Essentially, Treasury concluded that the entire on-site substation of a commercial System was energy property, while all equipment after the on-site substation (i.e., the gen-tie line) was transmission equipment⁶. Treasury’s position is generally consistent with the industry, and we understand consistent with how most assessors approach the issue for California Section 73 purposes. Thus, we recommend that the Guidance clarify that, in general, equipment up to and including the on-site sub-station will not be considered to be equipment for the transmission of electricity (and thus eligible for the exemption under Section 73 if such equipment otherwise meets the requirements for exemption) while, in general, equipment after the on-site substation will be considered to be equipment for the transmission or use of electricity (and thus ineligible for the exemption under Section 73).

DEFINITIONS – ELECTRICAL CORPORATION:

The Guidance explains that the Section 73 exemption only applies to property subject to local, rather than State-level, assessment. In this regard a System that is at least 50 megawatts AND which is owned by an electrical corporation is subject to state, rather than local assessment. Thus, large commercial Systems (i.e., at least 50 MW) will only be subject to the Section 73 exemption in the event they are not owned by an electrical corporation. Therefore, the determination of whether an entity is an electrical corporation becomes critical in the context of larger commercial Systems.

² Internal Revenue Code of 1986, as amended

³ American Recovery and Reinvestment Tax Act of 2009

⁴ See Ch. 28, Laws 1991, effective May 14, 1991 (“For purposes of subdivision (c) of Section 73 of the Revenue and Taxation Code, as added by Section 1 of this act, it is the intent of the Legislature, in defining an “active solar energy system” that uses solar energy in the production of electricity, to define that term as “solar energy property” is defined by Section 48(l)(4) of the Internal Revenue Code of 1986 and Section 1.48-9(d)(3), (4), and (6) of Title 26 of the Code of Federal Regulations . . .”).

⁵ Treasury Regulation §1.48-9(d)(3)

⁶ Treasury Chief Counsel Advice Memorandum 201122018, 2011

The Guidance outlines the statutory definition of an electrical corporation under Section 218. In this regard, an electrical corporation excludes an entity “producing power from other than a conventional power source for the generation of electricity solely for ... sale or transmission to an electrical corporation or state or local public agency, but not for sale or transmission to others unless the corporation or person is otherwise a electrical corporation.”⁷ Thus, a solar electric generating facility will be subject to local assessment (and thus qualify for the Section 73 exemption) provided the following requirements are met:

1. The generation of electricity by an active solar energy system is considered the production of power from other than a conventional power source; and
2. Such power is sold or transmitted to an electrical corporation or state or local public agency entity.

It is well settled that solar power plants are non-conventional power sources⁸ and in this regard we are unaware of any assessors that consider solar electric generation to represent a conventional power source. Therefore, we believe it would be helpful for the Guidance to confirm this understanding, by making clear that electricity generated by solar sources represents the production of power other than from a conventional power source⁹.

Further, it should be noted that an electrical corporation also excludes any independent solar power producer¹⁰. For these purposes an independent solar powerproducer means a corporation or person employing one or more solar energy systems for the generation of electricity for any one or more of the following purposes:

1. Its own use or the use of its tenants; or
2. The use of, or sale to, not more than two other entities or persons per generation system solely for use on the real property on which the electricity is generated, or on real property immediately adjacent thereto¹¹.

FIRST BUYER EXCLUSION:

Section 73 was modified in 2008 to allow the active solar energy system new construction exclusion to be conveyed to the first buyer of a new building containing such a system, provided the owner-builder does not intend to use the building, provided the owner-builder has not received the new construction exclusion for such System, and provided the new buyer purchases the System prior to it becoming subject to reassessment to the owner-builder.

⁷ Section 218(b)(3)

⁸ See public utilities code Section 2805, which defines conventional power sources as nuclear, large hydro, and the combustion of fossil fuels.

⁹ See BOE letter #08-091 dated September 17, 2008 in which the BOE concluded that, because solar power is not listed as a conventional power source, it is therefore excluded from this definition and, thus, falls within the category of “other than a conventional power source” under Public Utilities Code section 218, subdivision (b).

¹⁰ Section 218(e)

¹¹ Section 2868(b)

While most assessors have properly applied the exclusion to all Systems, including roof top and ground mount systems, a few have questioned whether the exclusion applies to active solar energy systems that are not on new buildings. This matter was resolved by recent legislation which amended Section 73. Specifically, the legislative intent declared that newly constructed active solar energy systems that are constructed as freestanding (i.e., ground-mount systems) or parking lot canopies, or that are constructed as installations on existing buildings qualify for the exclusion.

Given the Legislature's confirmation of the broad application of the Section 73 exclusion, we recommend you make clear in the Guidance, including the First Buyer Exclusion section of such Guidance, that the exclusion applies to all Active Solar Energy Systems, regardless of whether it is newly constructed on a new building or existing building, on a parking lot or similar canopy or structure, or if the System is a freestanding ground-mounted system.

In addition, we suggest the Guidance address the matter of whether the construction in progress of a System being constructed for the System owner by a contractor is properly eligible for the Section 73 exclusion, without jeopardizing the eligibility of the final, completed System for such exclusion under Section 73. Specifically, we believe the amount of any construction in progress ("CIP") of a System should be subject to the Section 73 exclusion, provided the System is being constructed for the owner by a contractor pursuant to a construction contract, and that the claiming of a Section 73 exclusion with respect to such CIP will not undermine the owner's ability to claim the exclusion under Section 73 for the full System, upon construction of such System.

TYPES OF USES FOR SYSTEMS – ELECTRICAL GENERATING SYSTEMS – COMMERCIAL OR INDUSTRIAL

Page 14 of the Guidance includes just three sentences of discussion regarding commercial and industrial electric generating Systems, even though these systems represent the majority of investments covered by the Section 73 exclusion. We believe this discussion should be expanded and adjusted to address the following:

1. The Guidance refers only to Systems that "provide a significant amount of the daily energy requirement of the building on which they are installed." However, as properly explained elsewhere in the Guidance, the Section 73 exclusion is not limited to Systems where the energy will be consumed on-site. Thus, this statement is overly narrow and could be misleading. Instead, the Guidance addressing commercial and industrial Systems should reflect the full scope of the exclusion, including Systems where the electricity is expected to be used on-site, sold to an off-taker, or used in some other qualifying manner.
2. The commercial and industrial discussion refers only to Systems on "buildings." However, as stated and as re-confirmed by recent legislation, the exclusion applies to all types of Systems, whether they physically rest on a building or are on a free-standing (i.e., ground mounted) basis, or upon some other set up (such as on car ports). Given that so many commercial and industrial Systems are either free-standing or based on alternative structures (such as car ports), we suggest the Guidance expand its discussion

to refer to these other Systems too, to ensure that there is no confusion regarding the proper scope of the Section 73 exclusion.

Should you have any questions or require additional information please do not hesitate to contact me.

Sincerely

Daniel Nelson

Daniel Nelson
Vice President, Tax