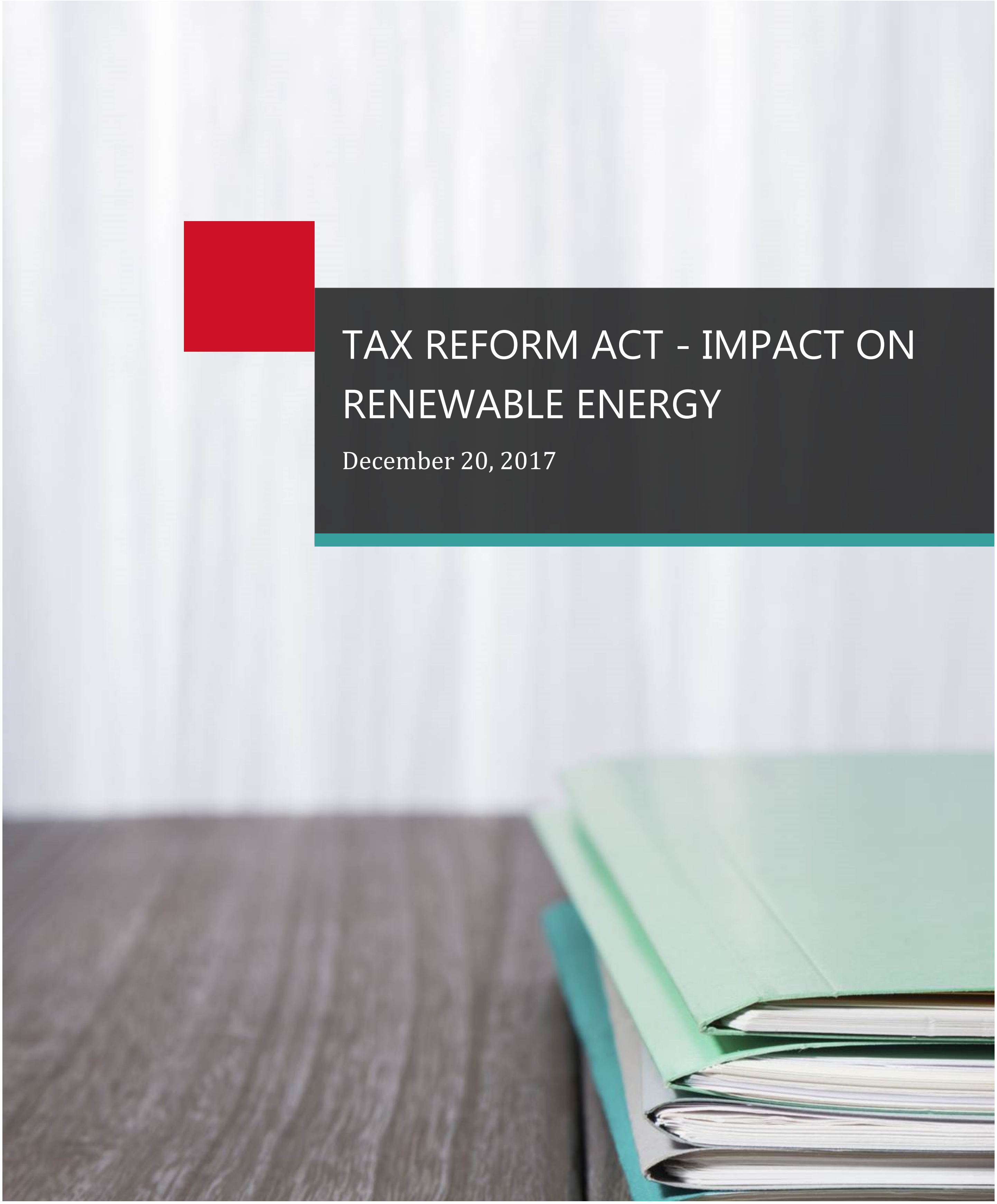

TAX REFORM ACT - IMPACT ON RENEWABLE ENERGY

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Tax Reform Act - Impact on Renewable Energy

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The Act (formerly known as the Tax Cuts and Jobs Act or the “Act”) makes sweeping changes to the Internal Revenue Code of 1986, as amended (the Code), and this update summarizes certain effects of the Act on taxpayers in the renewable energy sector. Should you have any questions or concerns about this update or how the Act may impact your business, please contact any of the authors of this update.

Executive Summary

- The production tax credit (the PTC) of Section 45 of the Code and the investment tax credit (the ITC) of Section 48 of the Code are left unchanged by the Act.
- The Act did not adopt proposed changes to the "continuous construction" requirement for determining when construction of a project commences.
- The corporate Alternative Minimum Tax (the AMT) will be repealed, ensuring that renewable tax credits will continue to be valuable to corporate investors.
- The new Base Erosion Anti-Abuse Tax (the BEAT) will limit or eventually eliminate the value of the PTC and ITC for certain multinational investors.
- The Act effectively eliminates the income deferral benefits of using prepaid power purchase agreements that are common in solar rooftop deals.

Renewable Tax Credits Unchanged

The House version of the Act included a number of proposed changes to renewable tax credits. It eliminated inflation indexing for the PTC and eliminated the ITC for solar energy projects for which construction commences after 2027. The final version of the Act does not adopt these proposals, leaving the PTC and the ITC unchanged.

Additionally, the House version of the Act would have codified the "continuous construction" requirement for determining when construction of a project commences. This requirement is currently established in IRS guidance, but such guidance also provides a safe harbor for projects placed in service within a certain time frame after construction commences. The House bill omitted, and thus would have invalided, the safe harbor. The final version of the Act did not include this proposal, so taxpayers may continue to rely on the safe harbor.

Under current law, the PTC and ITC are phased out based on when construction begins. The PTC and ITC for wind facilities are scheduled to phase-down for projects commencing through 2019, after which the credits expire. The ITC for solar properties phases-down through 2021, bottoming out at 10% for projects that commence after 2021. During the drafting process of the Act, several members of Congress indicated interest in extending these credits, but no extensions were included in any version of the Act. Any extensions of renewable tax credits will need to be part of a future extender package.

Repeal of the Corporate Alternative Minimum Tax

The Act adopts a corporate tax flat rate of 21% (reduced from the current maximum rate of 35%) and repeals the corporate AMT, effective January 1, 2018. The AMT imposed a minimum tax of 20% on certain corporations and restricted the use of the PTC to offset such tax. Repeal of the AMT ensures that the PTC will continue to be fully monetizable by most investors under the lower corporate tax rate (unless the taxpayer is subject to the BEAT provisions, as discussed below).

The Senate version of the Act had retained the AMT, raising alarm from the renewables sector. Under the lower corporate tax rate, the number of corporations subject to the AMT would have sharply increased, and the value of the PTC for such corporations would have been severely curtailed. The Act therefore avoids this undesirable result by repealing the AMT.

The Base Erosion Anti-Abuse Tax

The BEAT is a new minimum tax intended to prevent "earnings stripping" by multinational corporations. The BEAT minimum tax amount is computed each year and is generally the excess of (a) a percentage (generally 10%) of the taxpayer’s "modified taxable income" (generally, income computed without regard to certain "base erosion" payments made to foreign subsidiaries), over (b) the taxpayer’s regular tax liability reduced by its tax credits, *except* for certain business tax credits, including up to 80% of the value of the PTC or the ITC. In effect, the Act allows the taxpayer to offset any tax owed under the BEAT by 80% of the value of the PTC and the ITC. The Act does not provide a carry-forward mechanism to allow unused tax credits to offset the BEAT in future taxable years.

Whether and to what extent a corporation will be subject to the BEAT will not be certain until the end of each taxable year because the determination turns on a complex set of factors unique to each taxpayer. Thus, the value of the PTC or ITC in any given year is also uncertain. Creating additional uncertainty, the BEAT provisions relating to renewable credits expire after 2025. After 2025, the renewable credits provide no offset to the BEAT, which will vastly decrease the value of the credits for many investors in the tax equity market.

This result is in some respects more favorable to investors than the Senate bill’s original version of the BEAT, which did not include any adjustments for the PTC or ITC. But the final version may still negatively impact the tax equity market by reducing and eventually eliminating the value of the PTC and ITC for certain investors. Moreover, as compared to the Senate version, the final version of the Act expands the number of taxpayers that may be subject to the BEAT. How much the BEAT will affect corporate investors and the tax equity market overall is difficult to predict.

Prepaid Power Purchase Agreements

Under current law, prepaid power purchase agreements are often used in renewable projects (notably, in rooftop solar projects). This is because, in part, they permitted the electricity provider to include the advance payments in income over the entire period in which the electricity will be delivered. However, the Act will require these prepayments to be reported immediately as income (or, at best, partly in the year of the prepayment and partly in the following year, depending on the circumstances).

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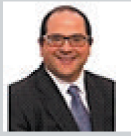

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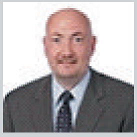

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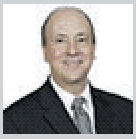

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