

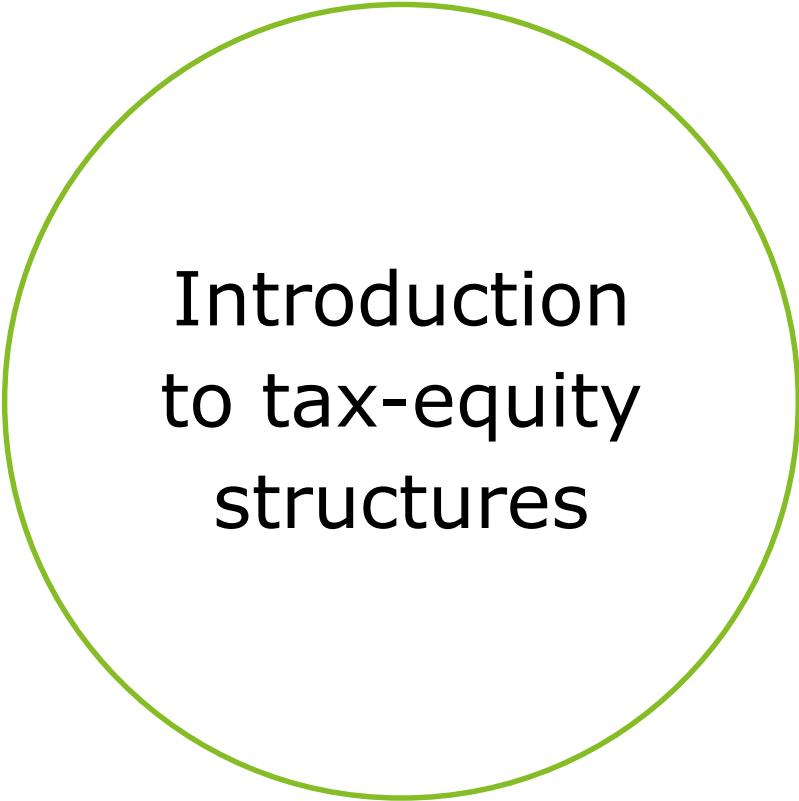


## 2017 Deloitte Renewable Energy Seminar

Innovating for tomorrow

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Energy Solutions



Introduction  
to tax-equity  
structures

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# Tax incentives are integral to project economics

What if I can't monetize the incentives currently?

- 1-year carryback / 20-year carryover period
- Multiple monetization structures are utilized
  - Partnership flip
  - Sale-leaseback
  - Inverted lease

# Partnership flip

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Participant	Role
1. Tax Investor	<ul style="list-style-type: none"><li>• Possesses sufficient taxable income to monetize tax benefits (both tax credits and accelerated MACRS tax depreciation)</li><li>• Subject to Passive Activity rules?</li><li>• Funds a percentage of total project costs</li><li>• Target IRR earned through allocation of 99% of tax credits and taxable losses/income and distributable cash</li><li>• Typically exits the project after the flip when the Developer/Sponsor exercises FMV purchase option</li></ul>

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# Partnership flip

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## Participant

## Role

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### 2. Developer / Sponsor

- ROI earned through cash flows, minimum 1% allocation of tax benefits and long-term ownership
  - FMV purchase option on Tax Investor's residual interest
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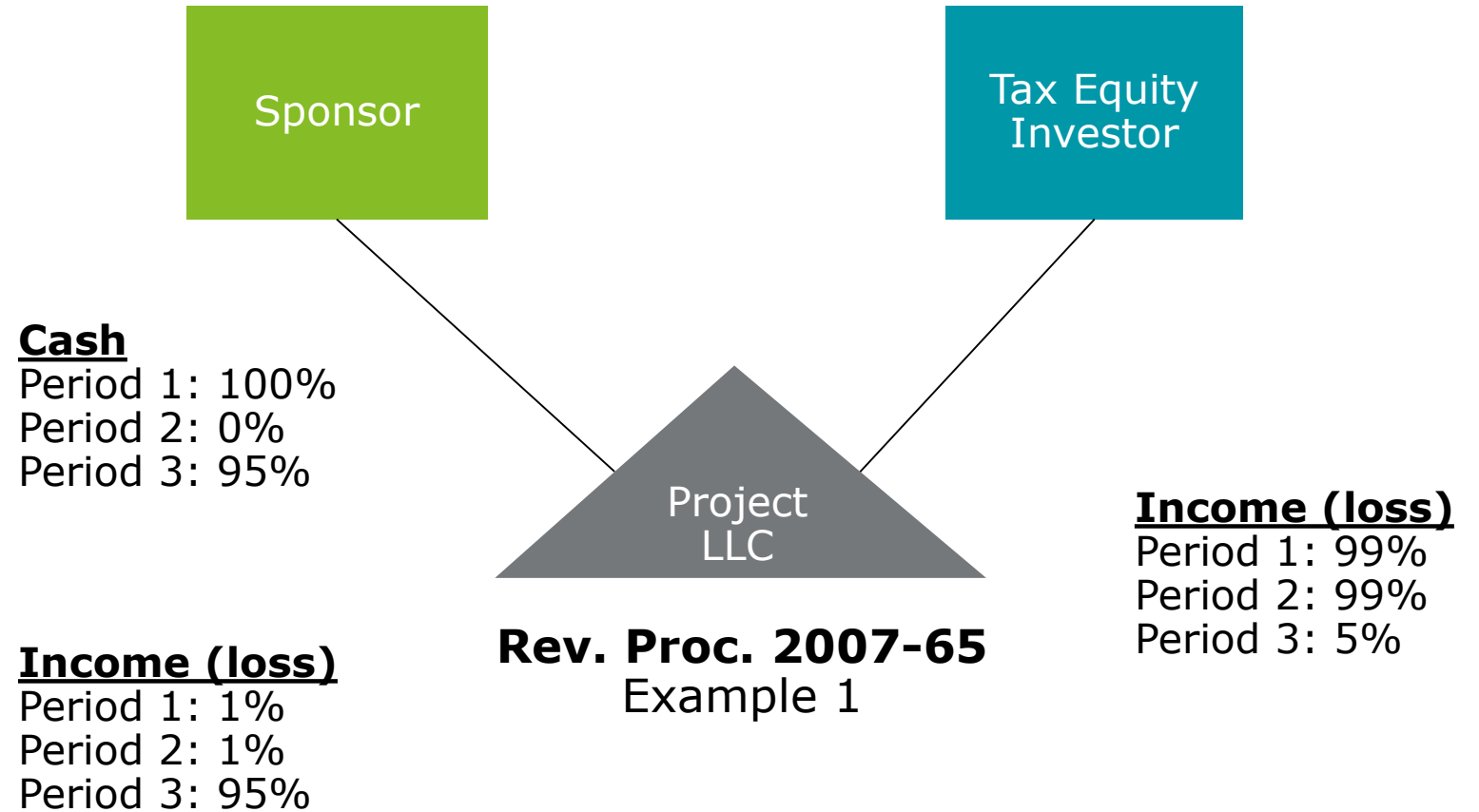
# Partnership flip

## IRC Section 45 PTC

- In order to claim the PTC, taxpayer must be the owner of the assets and the producer of the electricity
- Leasing structures not available (except for biomass)
- Partnership can be both owner and producer
  - Partnership special allocation rules are utilized to specially allocate the incentives to an investor
- Safe Harbor for wind PTC flip (Rev. Proc. 2007-65)

# Partnership flip

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1. PTC vs. ITC
  2. Rev. Proc. 2007-65
  3. Capital accounts
  4. Deficit restoration obligation (DRO)
  5. Cash-on-cash return
  6. Debt (project level vs. back-leverage)
  7. Tax-exempt ownership
  8. HLBV accounting



# Is the tax investor a valid partner?

Must assure that the partnership owns the assets and the partners own their interests

Rev. Proc. 2007-65

- *Historic Boardwalk Hall, LLC v. Commissioner*

Rev. Proc. 2014-12

Does the Tax Investor have enough upside and downside to be the tax-law owner?

Cash-on-cash return?



## Partnership flip structure with PTCs

Ownership structure and allocations must be respected for Federal income tax purposes

- Safe Harbor only applies to wind PTC partnership flips (Rev. Proc. 2007-65)
- IRS released ILM 201524024, 6/12/15, stating Rev. Proc. 2007-65 does not apply to ITC deals.

No recapture provisions or limitations on PTC to tax exempt or foreign investors (must be US project to qualify for PTC)

Depreciation limitations

- MACRS may be limited if tax exempt ownership in structure

# Partnership flip with ITC

In general, the same basic concepts as PTC flip structures

Partnering prior to commercial operation date is required

Ownership structure and allocations must be respected for Federal income tax purposes, however, no safe harbors

Recapture of ITC during first 5 years

- Vests 20% per year
- Grant in lieu of ITC has favorable recapture rules
- Partnership 1/3, 2/3 rules

# Partnership flip with ITC

Potential limitation of ITC if tax exempt ownership in structure

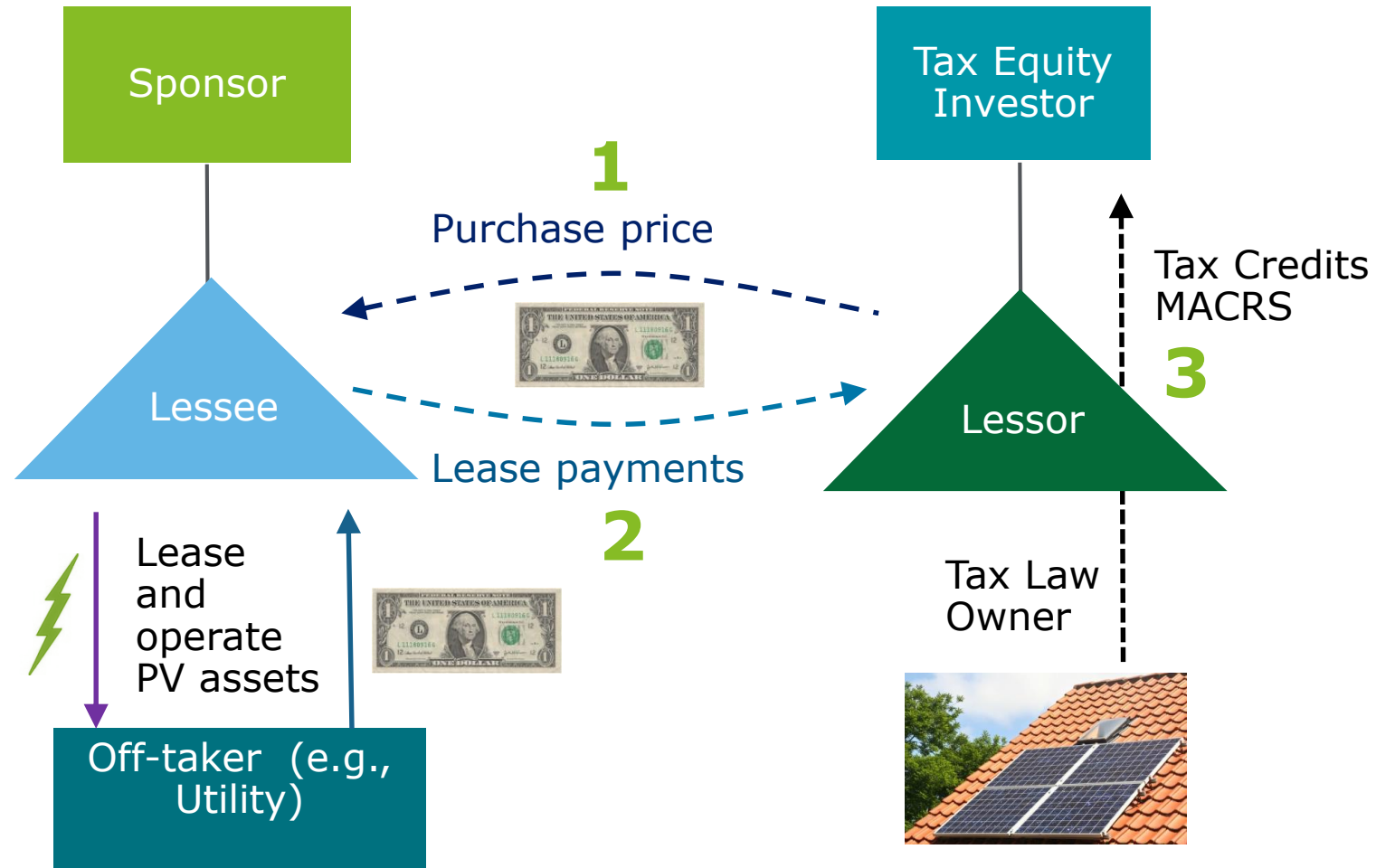
- Deal by deal consideration and potential impacts of blocker corporations

Basis reduction

- Depreciable (inside) basis must be reduced by 50% of the ITC benefit
- Outside basis of partnership interest must be reduced by the same amount

# Sale-Leaseback

1. Tax Investor (Lessor) purchases the installed panels from Sponsor (Lessee)
2. Sponsor (Lessee) leases back the solar project
3. Tax Investor will receive the 30% Investment Tax Credit based upon the purchase price and accelerated depreciation



# Tax Basics – Sale Leaseback

Time Period	Developer/Operator (Lessee)	Tax Investor (Lessor)
Construction Period and Placed in Service	(Project Development Costs)	
Sale of Project (90-Day Rule) and Lease Agreement	FMV Purchase Price ( <u>Project Development Costs</u> ) Gain on disposition	(FMV Purchase Price) <u>x 30%</u> ITC
Operations During Tax Credit Period	PPA Revenue (Rent) (O&M)	Rent (Depreciation) (P&I on acquisition indebtedness)
Exit	(FMV Purchase Price = 20% residual value)	FMV Purchase Price = 20% residual value

# Tax Basics – Sale Leaseback

## Significant Tax Issues

Tax ownership / true lease vs. financing characterization

- Lease vs. loan
- Lease vs. partnership
- Substance and form

90-day rule

Tax credit recapture

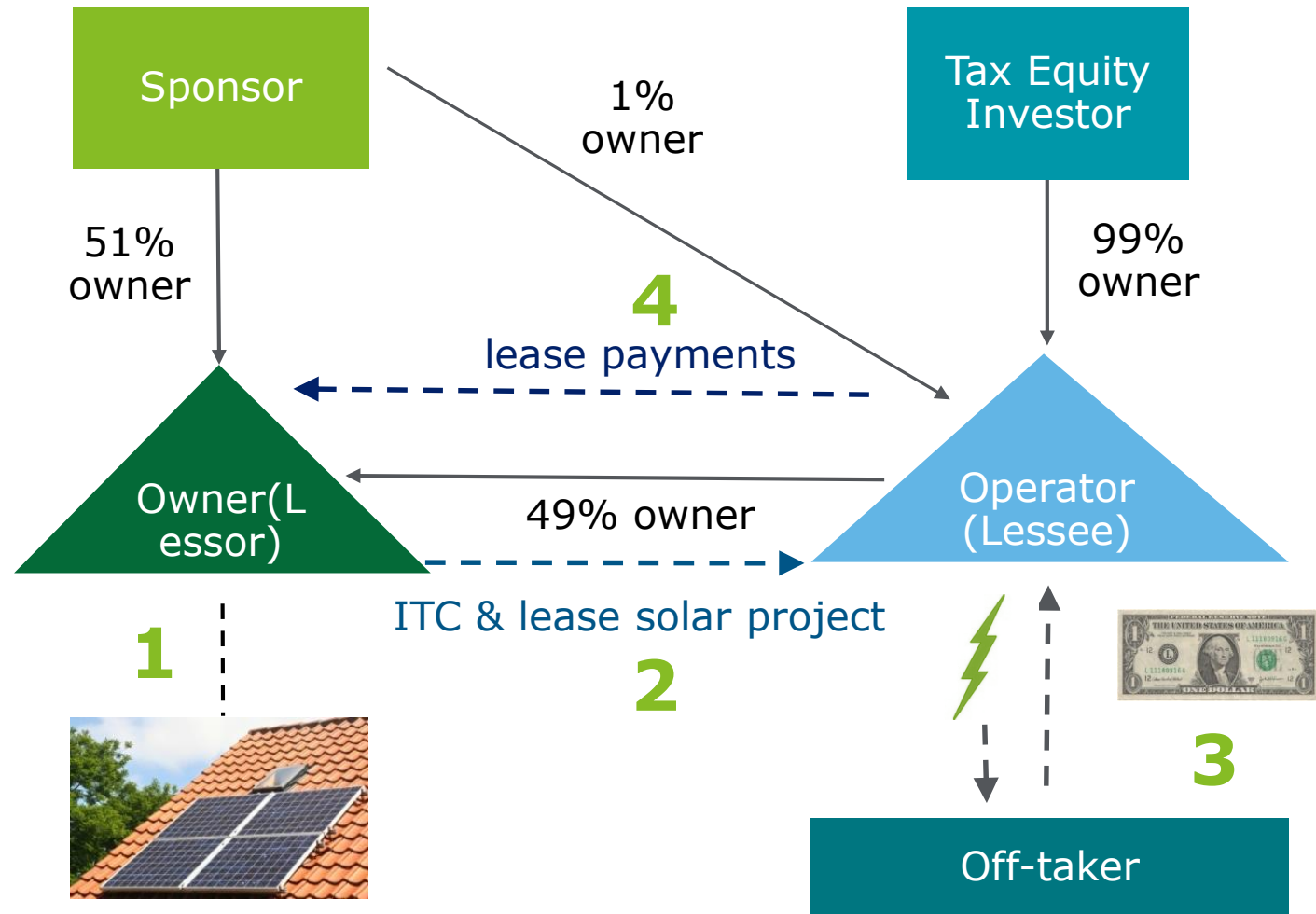
Basis reduction = 50% of credit

Tax-exempt use property

Structuring with ARRA 1603 grants

# Inverted Lease

1. Owner obtains long term lease rights and installs solar panels
2. Owner leases the panels to Operator & makes election to pass through credits to Operator as lessee; 99% of credits allocated to Tax Investor
3. Operator enters into Power Purchase Agreement to sell electricity from panels
4. Operator makes annual lease payments to Owner to cover debt service



# Tax Basics – Inverted Lease

Time Period	Developer/Operator (Lessee)	Tax Investor/Operator (Lessee)
Construction Period and Placed in Service	(Project Development Costs)	
Transfer Possession under LT Lease / 48(d) Election		"Deemed" FMV Purchase Price x30% = ITC
Operations During Tax Credit Period	Rent (Depreciation) (P&I on acquisition indebtedness)	PPA Revenue (Rent) (O&M)
Exit	(Greater of FMV of Member Interest or 20% Member Paid in Capital)	Greater of FMV of Member Interest or 20% Member Paid in Capital



# Tax Basics – Inverted Lease

Significant tax issues

Tax ownership / true lease vs. financing characterization

- Lease vs. loan
- Lease vs. partnership
- Substance and form

Lease pass-through election

Eligible basis – Valuation Issues

Income from basis adjustment

Partnership allocations

Tax credit recapture

Tax-exempt use property limitations

# Comparison – Sale Leaseback vs. Inverted Lease

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	Sale leaseback	Inverted lease
Financing	<ul style="list-style-type: none"><li>• Investor provides 100% financing (secured by PPA)</li></ul>	<ul style="list-style-type: none"><li>• Investor provides tax equity portion of financing (less project level equity and debt) (secured by PPA)</li></ul>
Exit cost	<ul style="list-style-type: none"><li>• Higher exit costs = 20% of expected FMV to purchase project at end of lease term (or FMV rent)</li></ul>	<ul style="list-style-type: none"><li>• Lower exit costs = Greater of 20% of Investor Member PIC or FMV of Member Interest</li></ul>
Operating Risk	<ul style="list-style-type: none"><li>• Insulates tax investor from operation risk by separating ownership from operations</li></ul>	<ul style="list-style-type: none"><li>• Tax investor takes on a share of operation risk but will seek to transfer this risk contractually to Developer through O&amp;M agreement</li></ul>

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# Comparison – Sale Leaseback vs. Inverted Lease

	Sale leaseback	Inverted lease
Technology risk	<ul style="list-style-type: none"><li>• Insulates Investor from technology risk since financing closes after placed in service date</li></ul>	<ul style="list-style-type: none"><li>• Tax investor has technology risk since financing must be closed prior to placed in service date</li></ul>
Basis Adjustment	<ul style="list-style-type: none"><li>• Tax investor benefits reduced by 50% basis adjustment (only 85% of property depreciated)</li></ul>	<ul style="list-style-type: none"><li>• Owner entity depreciates 100% of basis</li><li>• Tax investor recognizes 50% basis adjustment into income (offset by allocable share of 49% full depreciation and rent)</li><li>• Pre and post 50(d) regulations</li><li>• Increases the yield to Investor</li></ul>



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