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*Practice Groups:**Energy**Renewable Energy**Tax*

## Treasury Guidance Clarifies and (Again) Expands Field of Renewable Energy Projects That May Qualify for the PTC or ITC

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Notice 2017-04, issued on December 15, 2016, clarifies and expands the beginning of construction and continuity safe harbors applicable to certain alternative energy projects, including wind installations. Like Notice 2016-31, released on May 5, 2016, Notice 2017-04 concerns only projects that qualify for the Production Tax Credit (“PTC”) under Code Section 45 and, by extension, many projects that qualify for the Investment Tax Credit (“ITC”) through Code<sup>1</sup> Section 48(a)(5).<sup>2</sup> You may read more about the provisions and consequences of Notice 2016-31 in our [previous e-alert](#).

### Beginning of Construction Safe Harbor: Alternate Tests in Alternating Years

One of the pitfalls of Notice 2016-31 was that it stated that a taxpayer may not rely on the Physical Work Test and Five Percent Safe Harbor<sup>3</sup> in alternating calendar years to delay the “beginning of construction” test for the Continuity Safe Harbor. This limitation imposed a significant restriction on projects that were safe harbored in past years, but for various reasons had not yet been completed, because a new investor would be prohibited from “restarting” the continuous construction safe harbor period (see below) by investing additional capital or making further physical improvements. Notice 2017-04 provides helpful relief from that limitation by stating that the prohibition on alternate methods in alternating calendar years applies only to facilities for which construction began after June 6, 2016 (the date on which Notice 2016-31 was published). Thus, a taxpayer that began construction on a project in a prior year under the Physical Work Test, but first incurs five percent of the project cost in 2016 now has until December 31, 2020 to place the project in service.

### Expansion of Continuity Safe Harbor

Prior guidance in this area provided that, after timely beginning construction of an alternative energy facility, a taxpayer must be engaged in continuous construction (in the case of the Physical Work Test) or continuous efforts (in the case of the Five Percent Safe Harbor) in order to remain qualified for the PTC or ITC. Notice 2016-31 expanded the preexisting “Continuity Safe Harbor” by providing that a taxpayer would meet the continuous construction or continuous efforts tests if the taxpayer placed an eligible facility in service by the later of (1) the end of the fourth calendar year after the calendar year during which

<sup>1</sup> All references to the “Code” are to the Internal Revenue Code of 1986, as amended.

<sup>2</sup> Treasury stated in Notice 2016-31 and reiterated in Notice 2017-04 that the guidance provided in those Notices does not apply to the ITC claimed in connection with a solar facility. Guidance on that topic remains forthcoming.

<sup>3</sup> The Physical Work Test and Five Percent Safe Harbor are used to demonstrate that a taxpayer began construction of a qualifying alternative energy facility in time to qualify for either the ITC or the maximum amount of PTCs available in respect of such facility. You may read more about these tests in our [previous e-alert](#)

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construction of the facility began or (2) December 31, 2016. Now, under Notice 2017-04, a taxpayer will meet the continuous construction or continuous efforts tests if the taxpayer places an eligible facility in service by the later of (1) the end of the fourth calendar year after the calendar year during which construction began or (2) December 31, 2018. Thus, a wind facility that was safe harbored in 2013 pursuant to Notice 2013-29 may now qualify for the maximum PTC or ITC credit rates so long as the facility is placed in service by the end of 2018. As a result, Notice 2017-04 is of even greater value than Notice 2016-31 to owners of projects that have been safe harbored in past years, but the construction of which has been delayed.

### Cost of Improvements to Retrofitted Facilities Linked to Depreciable Basis

Notice 2016-31 also stated that the cost of retrofitting an eligible facility will qualify for the PTC and ITC provided that the fair market value of the remaining used property does not exceed 20 percent of the facility's total value after retrofitting (the "80/20" rule). However, Notice 2016-31 did not state how the cost of the retrofits should be calculated for purposes of evaluating qualification under the 80/20 rule. Notice 2017-04 clarifies that point by stating that the cost of new property includes all costs properly included in the depreciable basis of the new property. This characterization would include, for example, all tangible property that is necessary for the production of power (wind turbines, cables, inverters, and similar property), but not the cost of land. As stated in our [previous e-alert](#), it may be possible to leverage this guidance to obtain ITCs in connection with new energy storage property installed at existing qualified alternative energy facilities.

We invite you to contact the authors and any of the following K&L Gates LLP lawyers for more information about how Notice 2017-04 may impact your planned investments in the renewable energy space:

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