


Waning Tax Credits

MANAGING RENEWABLE ENERGY PROJECTS

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 **DESPITE EFFORTS BY INDUSTRY AND** many members of Congress, the extension of the largest subsidies for renewable energy projects, the Production Tax Credit and the Energy Credit, remain uncertain, with a December 31 expiration looming. A majority of renewable energy projects in development and under construction are economically viable in large part because of the availability of these tax credits. In order to qualify for the credits, a project must be placed in service, as defined under tax law, prior to the credit sunset date. Depending on specific circumstances, developers of projects that are at risk of not meeting the December deadline may want to consider accelerating the full project, or re-sequencing construction in order to bring at least a portion of the facility into service to qualify for some quantity of credits. Developers contemplating these alternatives should consider several factors, including the potential risks and the incremental costs of these approaches against the loss of credits in the event that the credits expire before the project is placed in service.

An electric generation facility is generally treated as placed in service for tax purposes if it meets several requirements including: it has received approval of required licenses and permits; it has been transferred to the control of the taxpayer; it has completed its critical tests; it has commenced daily or regular operations; and it has been synchronized to a power grid for transmission of the power produced. While there are some minor steps that a developer can take to accelerate the placed-in-service date for a project, such as by adjusting testing schedules, overall project timing cannot be materially affected without taking more significant actions like construction acceleration or re-sequencing.

Construction acceleration is generally achieved by increasing or re-allocating resources to reduce construction duration. Typical methods include increasing overtime hours, adding crews or adding shifts. Alternatively, it might be possible to re-sequence work in order to complete at least a portion of the project that would be eligible for the credits.

Adding overtime hours is often the fastest and most economical means to accelerate work, as it can be done quickly and does not require recruiting or on-boarding costs. To be cost-effective, however,

overtime generally needs to be limited in its duration and application. Studies by the Business Roundtable in 1980 and by others indicate that extended periods of overtime, typically more than eight weeks, can result in productivity deterioration such that overall output is no greater than would have been achieved with standard 40-hour workweeks. In addition to this erosion of productivity, safety incidents and absenteeism frequently increase as a result of fatigue and low morale. Consequently, although it is typically difficult to implement in practice, the optimal use of overtime is generally specific to activities on the schedule's critical path and for limited periods of time.

Accelerated construction can also be achieved by increasing the number of workers on existing shifts or by adding additional shifts. Adding labor, however, will result in increased costs and may not be a viable approach where there is a tight labor market. Comprehensive revised planning can prove to be critical when accelerating in this manner because stacking of trades, overcrowding and logistical challenges can lead to reduced productivity, escalating costs and construction claims by contractors.

Another approach is to re-sequence the work to bring a portion of the generation plant online by the December 31 deadline. To meet the tax placed-in-service requirements, the portion of the project that is placed online must not only meet the five-part tax placed-in-service test, it must also be deemed to be a discrete facility and not interdependent with the remainder of the project. Re-sequencing will require a revised schedule and budget for several reasons, including defining the new critical path and identifying expedited material or equipment needs. This revised schedule and budget can allow the developer to weigh additional project costs against the value of obtaining the credits.

Irrespective of the approach selected to meet the expiration, the developer should consult with project schedulers and engineers to evaluate and track changes to the critical path. Special attention should be given to understanding whether the proposed schedule changes result in conflicts with ancillary construction activities; whether key resources could become constrained; and the degree to which activities that cannot be reasonably accelerated – for example, curing concrete – are on the critical path. Additionally, the developer and the contractor should consider executing the terms of schedule modifications to prevent future disputes. Finally, the cost and value of undertaking any of these steps should be weighed against either the potential for failing to qualify for the credit or for any potential incremental increases in financing costs associated with that uncertainty.

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