IRS Issues Favorable PLR Allowing an Individual Panel Owner in an Offsite, Net-Metered Community-Shared Solar Project to Claim the Section 25D Tax Credit

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The Internal Revenue Service has issued a private letter ruling to an individual owner of solar panels installed in an offsite net-metered community-shared solar project confirming the individual's eligibility for the income tax credit under Section 25D of the Internal Revenue Code. A redacted copy of the PLR is **available here**. (As of the date of this Alert, the IRS has not provided its release number for the PLR.) This PLR provides significant insight into the IRS view on the application of Section 25D to community-shared solar projects. Foley Hoag attorneys **Nicola Lemay** and **Adam Wade** provided the legal work to obtain the PLR on behalf of its clients, the individual taxpayer and the Clean Energy States Alliance (CESA).

The Section 25D Tax Credit

Section 25D allows individual taxpayers a federal income tax credit equal to 30% of the qualified solar electric property expenditures made by the taxpayer. The term "qualified solar electric property expenditure" generally means an expenditure for property which uses solar energy to generate electricity for use in the individual taxpayer's residence within the United States. The Section 25D tax credit is the income tax credit that typically is claimed by an individual taxpayer who purchases a rooftop solar system for his or her residence directly from an installer.

Prior Section 25D Guidance

Interpretations before 2013 suggested that the Section 25D tax credit was only available for expenditures incurred for onsite (e.g., rooftop) installations. In Q/A-26 of Notice 2013-70, released November 18, 2013, the IRS clarified that the Section 25D tax credit potentially could be available for expenditures incurred for net-metered offsite solar installations. The practical impact of the Notice for structuring community-shared solar projects has been limited, however, because the Notice only addresses a narrow scenario in which (i) the offsite solar installation is 100% owned by a single individual taxpayer, and (ii) the individual taxpayer enters into a net-metering contract with the local utility that specifically recites that the taxpayer retains legal title to electricity generated by the offsite solar installation until it is delivered to the taxpayer's residence. Many, if not most, net metering laws and tariffs do not address title to electricity in this way.

Significance of the PLR

The new PLR provides written clarification of the IRS's view on the availability of the Section 25D tax credit for offsite, net-metered community-shared solar installations. In particular, the PLR clarifies that (i) an offsite solar installation that includes solar panels owned by an individual taxpayer, as well as solar panels owned by other individuals, potentially can qualify for the Section 25D tax credit, and (ii) an allocation of net metering credits by the offsite solar installation to an individual taxpayer's residential utility bill that is based on the number of solar panels in the installation that are owned by the individual and that is generally sized to approximate the amount of such bills can satisfy Section 25D's requirement that the electricity generated by the solar property be used in the individual taxpayer's residence. It should be noted that the PLR assumes that the offsite solar installation and the taxpayer's residence are located in the same state and subject to the jurisdiction of the same public utility.

Significance of the Section 25D Tax Credit for Community-Shared Solar

Taking into account the Section 25D tax credit, individuals who are able to fund the upfront costs of acquiring direct ownership of solar assets (whether through personal cash savings, home equity lines of credit or other emergent solar-specific individual financing) may be able to realize greater value and shorter payback periods than the economics offered under third-party solar power purchase agreements (PPAs) or lease transactions.

Pairing the value of the Section 25D tax credit with the lower installed cost and economies of scale offered by community-shared solar holds tremendous potential to further enable direct ownership of solar assets by individuals in utility territories with supportive net metering programs.

Community-shared solar is not defined by any one particular type of transaction or financial structure. Many community-shared solar transactions, for example, have made successful use of the 30% business investment tax credit under Section 48 of the Internal Revenue Code. However, the use of the Section 48 tax credit for community-shared solar transactions has clear limitations. The Section 48 tax credit is typically unavailable directly to individual taxpayers because it is a business tax credit, and individuals' indirect access to the tax credit through investment in an entity that owns a community-shared solar installation is complicated by limitations on the ability of individuals to use tax credits derived from passive activities and "accredited investor" requirements. Further, to monetize the Section 48 investment tax credit, developers generally must negotiate complex transactions with third-party tax equity investors. With the insights offered by the new PLR, individual taxpayers who acquire direct ownership of solar panels in a properly-structured offsite community-shared solar transaction may have an opportunity to approximate what may have been gained had they been able to benefit from the Section 48 tax credit.

Legal Status of the PLR

Under the specific facts presented in the PLR, the IRS has agreed with the individual taxpayer that his or her purchase of solar panels that are part of an offsite, net-metered community-shared solar installation qualifies for the Section 25D tax credit. Community-shared solar project developers and individuals should review the PLR with their own tax counsel, accountants, and tax preparers in light of their own specific facts. Although, by law, this PLR cannot be used or cited as precedent by other taxpayers, several cases acknowledge that a private letter ruling can be used as 'persuasive authority' or an 'instructive tool' by courts, IRS personnel and practitioners. In general, private letter rulings also may be used by the IRS in its own interpretations, including by IRS employees who might consider it in issuing private letter rulings to similarly situated taxpayers.

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