

# New York Governor Proposes NY-SUN Initiative and Tax Benefits

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New York Gov. Andrew Cuomo (D) recently unveiled the NY-SUN Initiative, an ambitious energy plan aimed at significantly expanding by 2013 the amount of energy produced in New York by means of solar energy. Cuomo seeks to expand and upgrade New York's electrical power grid and to invest considerable resources in the development of solar power.

In particular, the NY-SUN Initiative would expand the residential solar energy system equipment credit against individual income tax under section 606(g-1) of the New York Tax Law to include a credit for payments made under some leases of solar energy system equipment or agreements to purchase solar power. The NY-SUN Initiative would also expand the exemption from the New York sales and use taxes available to the retail sale and installation and use of residential solar energy systems equipment to the acquisition of that equipment by commercial enterprises, such as retailers and hotels. Local governments also would be provided with the option to offer the same exemption from their local sales and use taxes.

The proposed amendments to section 606(g-1) are contained in Part H of the governor's 2012-2013 New York State Executive Budget, Revenue Article VII Legislation.

## Background to the Current Solar Energy System Equipment Credit

Under current New York law, an individual taxpayer is allowed a credit against her New York individual income tax equal to 25 percent of her qualified solar energy system equipment expenditures (that is, expenditures for materials and labor costs properly allocable to on-site preparation, assembly and original installation, architectural and

engineering services, and designs and plans directly related to the construction or installation of solar energy system equipment, but excluding interest and other finance charges), up to a maximum credit of \$5,000. For purposes of determining the amount of expenditures incurred in purchasing and installing solar energy system equipment, those expenditures are reduced by the amount of any federal, state, or local grant received by the taxpayer that was used for the purchase or installation of that equipment and is not included in the federal gross income of the taxpayer.

The credit is allowed for the tax year the solar energy system equipment is placed in service. If the credit exceeds the taxpayer's tax liability for that year or successive years, the remaining amount of the credit may be carried over for an aggregate of five tax years.

To be eligible for the credit, a taxpayer must purchase solar energy system equipment (excluding equipment that is also used in a non-solar energy system, such as an oil or gas distribution system, or is used to heat a swimming pool or other recreational facilities) and install it at the taxpayer's principal residence in New York. The maximum capacity for that system is 25 kilowatts per residence, and 50 kilowatts for condominiums or co-operatives. A taxpayer's principal residence is the home where the taxpayer and her family lives most of the time, and excludes a summer or vacation home.

The credit is not subject to recapture, even if the taxpayer no longer uses the residential property where the equipment is installed following the date that equipment is placed in service. If the taxpayer moves from one principal residence to another principal residence in New York, a separate credit is allowed for each principal residence, so long as the costs for the solar energy system equipment are incurred by the taxpayer when the residence is her principal residence and the credit is claimed (subject to the carryover rules) in the tax year the equipment is placed in service.

The current law provides special rules if multiple taxpayers share a principal residence, or solar energy system equipment is purchased by a condominium or cooperative. If solar energy system equipment is purchased and installed in a principal residence shared by two or more taxpayers, the total amount of the credit allowable for each taxpayer is prorated according to the percentage of the total expenditure for such equipment contributed by each taxpayer. Similarly, if solar energy system equipment is purchased and installed by a condominium management association or a cooperative housing corporation, a taxpayer who is a member of that association or a tenant-stockholder in the corporation may claim a proportionate share of the total expenditure attributable to her principal residence.

### **Proposed Tax Incentives Under the NY-SUN Initiative**

Cuomo's proposal would expand the definition of qualified solar energy system equipment expenditures to include an amount equal to all payments made during the tax year by a taxpayer for the lease of solar energy system equipment (owned by someone other than the taxpayer) or the purchase of power when that power is generated by solar energy system equipment (owned by someone other than the taxpayer). The equipment must be installed at a residential property in New York that is the taxpayer's principal residence when the solar energy system is placed in service.

### ***It is unclear how the current carryover rules would apply to any amount of unused credit.***

To be eligible for the credit, the taxpayer's lease or power purchase agreement must be written, and span at least 10 years. Importantly, unlike the credit available for purchases of solar energy system equipment, the credit available for payments made under a lease or power purchase agreement is limited to 12.5 percent, half the 25 percent provided for purchases of that equipment under current law. However, it appears that the proposed credit is available in each tax year payments are made under a lease or a power purchase agreement, not just in the tax year the equipment is placed in service. It is unclear whether the credit for payments made under a lease or power purchase agreement is subject to the current maximum amount of \$5,000, or how the current carryover rules would apply to any amount of unused credit. Also, it appears that the amendments to the definition of solar energy system equipment sunset on January 1, 2015; however, the proposal is unclear regarding whether that sunset date is generally applicable to all amendments that the governor proposed.

The NY-SUN Initiative would also expand the exemption from the New York sales and use taxes available to the retail sale (including the transfer of possession but not title under a rental or lease agreement) and installation and use of residential solar energy systems equipment to the acquisition of that equipment by commercial enterprises, such as retailers and hotels. For purposes of this exemption, solar energy systems equipment means equipment using solar radiation to produce energy designed to provide heating, cooling, hot water, or electricity in a building or a structure, but excludes equipment that is part of a non-solar energy system or equipment used to heat residential swimming pools. Such equipment cannot have an installed capacity rating that exceeds two megawatts. Local governments also will be provided with the option to offer the same exemption from their local sales and use taxes.

If enacted, the proposals would take effect immediately, provided that the credit for leases and purchases of power under written agreements would apply only to agreements entered into on or after such effective date. The amendments to state and local sales and use tax would apply to sales made or uses occurring on or after September 1, 2012.

### **Comments on the Proposed Tax Incentives Under the NY-SUN Initiative**

We believe that the proposed tax incentives under the NY-SUN Initiative — as currently written — are likely to provide a significant increase in expenditures on solar energy system equipment and the development of New York's solar power system. We also believe that some clarifications to the tax incentives would further enhance the long-term success of the NY-SUN Initiative. Our recommended clarifications for the final legislative text are as follows:

- The final legislative text should clarify that because the credit available to lessees and purchasers of power is half the credit available to purchasers of solar energy system equipment, the amount of the credit is not subject to the \$5,000 limitation contained in the current law. If the \$5,000 limitation is applicable, it should be clarified whether there is any limitation regarding how much of the consideration under a lease or power purchase agreement may be paid in a single year.
- The governor should consider proposing a term of less than 10 years for leases and power purchase agreements under which payments qualify for the credit. For example, requiring that leases or power purchase agreements span only five years in order for their payments to qualify for the credit would achieve the NY-SUN Initiative's goal of providing incentives for longer-term expenditures on solar energy system equipment while also committing taxpayers to a shorter term under which they

would be required to make payments in order to receive the credit. A shorter term would reduce the commitment period undertaken by a taxpayer when entering into a lease or power purchase agreement, which could in turn increase a taxpayer's willingness to enter into a lease or power purchase agreement and see whether solar power meets her energy needs and cost requirements.

- The final legislative text should clarify that the credit available to lessees and purchasers of power applies separately to each tax year in which payments are made under a lease or power purchase agreement and arises for those payments in each of those years (regardless of when the applicable solar energy system equipment is placed in service); that is, the credit should be 12.5 percent of each rent or power purchase agreement payment.
- The final legislative text should also clarify that the credit for each of those tax years, if not used in the tax year the credit first arises, will carry forward for five years, and that in each successive year the oldest credits carried forward will apply to reduce the amount of income tax due before any newer or new credits. For example, if H makes payments under a lease in the amount of \$100 in each of tax year 1 and tax year 2, H would be entitled to claim a credit equal to \$12.50 in tax year 1 and a separate additional credit of \$12.50 in tax year 2. H would be able to carry forward any unused amount of the credit from tax year 1 to, at the latest, tax year 6, as well as any unused amount of the credit from tax year 2 to, at the latest, tax year 7. Also, in tax year 2 and later, the remaining credit, if any, from tax year 1 would be applied to reduce H's income tax before the credit from tax year 2 would be applied. That means, depending on the amount of H's income tax in tax year 2 and the amount of her unused credit from tax year 1, that the credit from tax year 2 may not even be applied in tax year 2, the tax year in which it arises, but would in no case be carried forward beyond tax year 7.
- The final legislative text should clarify that the current rules applicable to the apportionment of the credit between taxpayers who share a personal residence, or are members of a condominium or tenant-stockholders in a cooperative, apply equally to the credit received for payments under a lease or power purchase agreement.
- The final legislative text should clarify to which part or parts of the credits the proposed sunset date of January 1, 2015 applies. If there is a sunset date for credits for payments made under a lease or power purchase agreement, we

believe that the credit for payments made under a lease or power purchase agreement that commenced before January 1, 2015 should not be subject to the sunset.

- We note that New York income tax law appears to follow U.S. federal income tax law in terms of characterizing a transaction as a true lease or an installment sale. See generally John Amato & Donna Fiammetta, *Equipment Leasing: State Income and Franchise Tax Considerations* (CCH 2001). It would be helpful to have that point confirmed, at least in the legislative history, so that New York taxpayers know that they may rely on IRS Revenue Ruling 55-540, 1955-2 C.B. 39, and *Frank Lyon Co. v. United States*, 435 U.S. 561 (1978), to determine whether they have a lease for purposes of this legislation.
- We note that the concept of a "power purchase agreement" is not defined in the legislative text. We believe that the final legislative text should clarify that a power purchase agreement is intended to be a "service contract," as defined in section 7701(e) of the Internal Revenue Code of 1986, as amended. However, if that is not the legislative intent, the final legislative text should provide a clear definition as to what constitutes a power purchase agreement.
- The final legislative text should clarify that payments made under a lease or power purchase agreement for solar energy system equipment installed at an individual's principal residence or at a place of business are also exempt from the state sales and use tax, and provide local governments with the option to offer the same exemption from their local sales and use taxes.

We praise the governor for unveiling the NY-SUN Initiative but encourage him and the New York State Assembly to enhance further the long-term success of the NY-SUN Initiative by undertaking the above-recommended clarifications in the final legislative text for the credits. In addition to providing tax incentives for the development of solar power in New York through credits to a New Yorker's individual income tax and exemptions from state and local sales and use taxes, the governor, New York State Legislature, and local communities should consider other alternatives for spurring the development of solar power in New York. Those alternatives could include providing businesses and commercial enterprises with credits against their New York franchise taxes for solar energy expenditures, as well as expanding real property tax incentives for individuals, businesses, and commercial and industrial enterprises that install solar energy equipment on their leased or owned real property and buildings or dwellings. ☆