



Alternative & Renewable Energy Tax Newsalert

Treasury's 1603 Grant Program: When can you use the "3 1/2 month rule" to take delivery of property in 2012 and still reach the 2011 construction safe harbor?

December 2, 2011

To be eligible for the Treasury 1603 grant program, companies must "begin construction" on their projects by December 31, 2011. Construction begins when a company either (a) incurs at least 5% of eligible project costs ("5% test") or (b) begins "significant physical work" in a plan of continuous construction. For potential applicants relying upon the 5% test, the important milestone is the date the costs are incurred. Where a project asset is produced, manufactured, or constructed for the applicant by another person, the cost of that asset is incurred when the property and/or services are provided to the applicant, under the "economic performance" test of Treas. Reg. §1.461-1. One notable exception to the economic performance general rule is Treas. Reg. §1.461-4(d)(6), which allows property or services that are reasonably expected to be provided within 3 1/2 months of the date of payment to meet the economic performance requirement when payment is made.

Many applicants facing the December 31st deadline to meet the 5% test have viewed these economic performance rules as allowing two options: (a) take delivery of eligible property and incur other eligible costs by year-end or (b) rely on the 3 1/2 month rule. Under the plain language of the regulation and Treasury's Begun Construction FAQ #17, this would allow an applicant to meet the 5% test on December 31, 2011 for property or services reasonably expected to be provided by April 15, 2012 assuming payment is made on December 31, 2011. (An

accrual method taxpayer also must have a fixed liability by December 31, 2011 in order for the amount to be "incurred.") In addition, this would apply to the determination of costs incurred by an applicant's accrual-method vendors under binding written contracts using the "look through" method of meeting the 5% test, *i.e.*, the vendor would incur costs on the payment date for equipment, supplies or services expected to be provided within 3 1/2 months.

However, Treasury officials recently have expressed the view that applicants relying on the "look through" method are bound by any accounting method elections their contractors have made in determining when eligible costs are incurred. While there is not clear guidance addressing whether the use of the 3 1/2 month rule for the 1603 grant program is a method of accounting, many consider it to be one. As such, the applicant or the applicant's vendor must be entitled to use this method, either as a method consistent with its existing method, or as a new entity or an existing entity engaging in a new trade or business that adopts the 3 1/2 month rule. Absent such conditions, the applicant or the applicant's vendor may be ineligible to use the 3 1/2 month rule and, thus, would need to have all assets, equipment, supplies or services actually provided by December 31, 2011 in order to "incur" the amounts and include them in the 5% test. If such costs are necessary to meet the 5% test, this could impact overall project eligibility for the 1603 grant program.



For more information

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