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Judicial Update

Alta Wind Court Order Offers Guidance on Valuation and Allocation Practices for Renewable Energy Projects

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On July 8, the U.S. Court of Federal Claims issued its post-remand decision in *Alta Wind I Owner Lessor C, et al. v. United States* (Alta Wind). This decision provides guidance on the valuation of renewable energy projects and the allocation of purchase price among tangible and intangible assets.

Alta Wind involves six California wind farms, the purchasers of which claimed cash grants under the now-expired Section 1603 of the Internal Revenue Code (the Code) established by the American Recovery and Reinvestment Act of 2009 and administered by the U.S. Department of the Treasury. The dispute focused on the portion of the facilities' purchase price properly allocable to grant-eligible tangible energy property, as distinguished from power purchase agreements, development rights, goodwill, going-concern value, the anticipated Section 1603 grants, and other intangible assets and attributes.

The litigation in this case has been ongoing for more than a decade and has resulted in multiple decisions by both the Court of Federal Claims and the U.S. Court of Appeals for the Federal Circuit. In 2016, the Court of Federal Claims largely accepted the project valuation methodology put forth by the taxpayer in Alta Wind. However, this decision was vacated by the U.S. Court of Appeals for the Federal Circuit in 2018, which held that the trial court had failed to properly allocate the purchase price among the acquired assets under Section 1060 and remanded the case for further proceedings. Following additional proceedings on remand, including a 2023 opinion concluding that the value of an anticipated grant under Section 1603 could not automatically be added to the basis of the project, the Court of Federal Claims issued its most recent decision, providing detailed guidance regarding the appropriate valuation methodology and the allocation of purchase price between grant-eligible tangible property and ineligible intangible assets.

Although Code Section 1603 is no longer in effect, the basic rules for valuation are largely the same as those used to determine the basis of energy property for the Investment Tax Credit (ITC) under Code Sections 48 and 48E. As a result, Alta Wind is expected to have significance beyond the Section 1603 program and will likely influence the valuation of ITC eligible projects, particularly in transactions involving purchased or recently developed renewable energy facilities. The key holdings in Alta Wind are outlined below.

The Taxpayer's Discounted Cash Flow Valuation is Rejected

The taxpayers in Alta Wind used the discounted cash flow (DCF) approach to value their projects, valuing each project by projecting its expected future cash flows and discounting those cash flows to present value. In calculating the expected future cash flows, the taxpayers included approximately 98% of the anticipated Section 1603 cash grant proceeds, which were valued at 30% of the projects' eligible basis. The court disagreed with the taxpayers' inclusion of the anticipated grant proceeds in the valuation of the projects, arguing that such an inclusion is circular. Because the Section 1603 grant equaled 30% of the eligible tangible property's basis, including the anticipated grant in the valuation used to determine that basis would increase the basis, which would increase the grant and, in turn, further increase the asserted basis. The court effectively stated that when valuing a project, a taxpayer should be able to demonstrate that the value calculated belongs solely to the eligible tangible property rather than to expected tax benefits and other intangibles.

Although the taxpayers attempted to use their selected discount rate to isolate tangible value from intangible value, the court found the deficiencies relating to the anticipated grant dispositive. Notably, the court did not hold that the DCF valuation is inherently improper; taxpayers may still use DCF valuation in situations with more evidentiary support.

Modified Cost Approach

The court adopted the government's cost approach with some modifications from the plaintiffs to value the projects. The court explained its methodology as follows: (i) begin with the cost segregation reports for the projects, (ii) exclude development rights and any independent turn-key premium, (iii) include the development fee and interest during construction as indirect costs, (iv) apply grant-eligibility ratios and (v) apply a market-supported developer profit.

Developer Profit

The court rejected the government expert's 9% developer-profit calculation. The expert used a capital asset pricing model but did not survey developers or analyze actual market transactions. The court concluded that the model effectively calculated a discount rate rather than developer profit.

Instead, the court relied on appraisals prepared by DAI, an independent appraiser that analyzed actual wind-farm transactions. DAI identified a developer-profit range of 15% to 30% for Alta II through V, a 20% rate for Alta VI, and a range of 10% to 15% for Alta I. Based on that market evidence, the court applied a 20% developer-profit rate to Alta II through VI and a 15% rate to Alta I.

While the developer profits percentages of 15-20% were specific to the Alta Wind projects and not intended as fixed industry standards, the decision reaffirms that a reasonable developer profit is appropriate to include in the fair market value of ITC-eligible property when supported by the facts. In addition, the court permitted the taxpayers to add to the construction cost (i) the interest paid on construction debt and (ii) fee paid to buy out the original developers.

No Separate Turnkey Premium

Turnkey value represents the additional amount a buyer will pay for an integrated, operational facility rather than a collection of separate components.

The court declined to add a separate turnkey premium to the cost-plus-developer-profit valuation in this situation because it concluded that the price of the turbine supply and balance-of-plant contracts already included that value. Those contracts required the contractors to deliver completed and operational facilities and allocated integration and completion risks through testing, commissioning, warranties and liquidated-damages provisions.

Accordingly, a taxpayer seeking an additional turnkey premium must demonstrate that the underlying contract prices do not already compensate the contractor for the same completion and integration risks. Otherwise, the additional premium would impermissibly double count the value of those risks.

Looking Ahead

The Alta Wind decision reaffirms that taxpayers bear the burden of demonstrating the evidentiary support for basis step-ups related to a project's acquisition, and particularly the allocation of the purchase price between eligible tangible property and intangible assets. This decision paints a clearer picture on the level and kind of scrutiny that may be placed on the valuation of grant-receiving projects or projects eligible for the ITC. It will likely cause financing parties and insurance carriers to scrutinize step-ups and cost segregation studies even more closely and possibly require appraisers and accountants to bolster the support for the determination of the amount of turnkey value attributed to ITC-qualifying projects.

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