

# Update on Section 1603 Treasury Grant Litigation

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# Update on Section 1603 Treasury Grant Litigation

## Background on Section 1603 Grants

- Enacted in Section 1603 of the American Recovery and Reinvestment Tax Act of 2009
- 10% or 30% cash grant is provided for renewable energy facilities in lieu of ITC or PTC
  - Facility must be placed in service in 2009, 2010 or 2011, or
  - Facility can be placed in service after 2011 if construction began in 2009-2011
- Solar, wind, biomass, geothermal, hydropower, landfill gas, trash, fuel cell, microturbine, and CHP, marine and hydrokinetic facilities.
- Application process.
- Applicants who receive a cash grant cannot also claim ITC or PTC
- Cash grant only available for property used in a trade or business or for the production of income

# Update on Section 1603 Treasury Grant Litigation

## Administration of Grant Program

- U.S. Department of Treasury, Office of the Fiscal Assistant Secretary (Treasury), administers the Grant Program.
  - Program Manager
  - Fiscal Affairs Specialist
  - Treasury's General Counsel
- Neither the Office of Tax Policy nor the IRS are directly engaged in the administration of the Grant Program.



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## Administration of Grant Program

- Treasury has contracted with the National Renewable Energy Laboratory (NREL) to perform the review of grant applications.
  - Section 1603 Review Team (assembled from outside NREL)
  - Primary Reviewer
  - Secondary Reviewer
  - Senior Reviewer
- Recommendations to Treasury
- Approval of awards by Treasury

# Update on Section 1603 Treasury Grant Litigation

## Status of Section 1603 Grant Program

As of December 31, 2015

- total number of projects funded = 104,211
- total §1603 funding = \$24.9 Billion
- total estimated private, regional, state, and federal investment in §1603 projects = \$90 Billion
- total installed capacity of funded projects = 33.3 GW
- total estimated annual electricity generation from funded projects = 88.7 TWh

Figure 1: Number of Projects by Type<sup>4</sup>

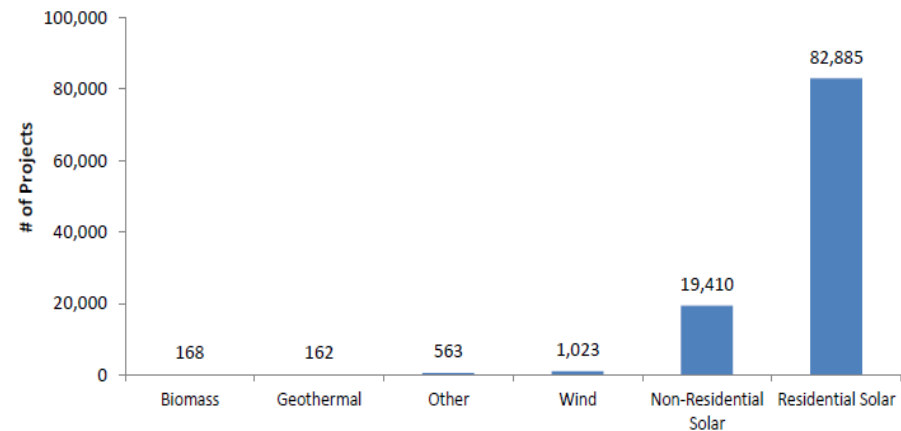
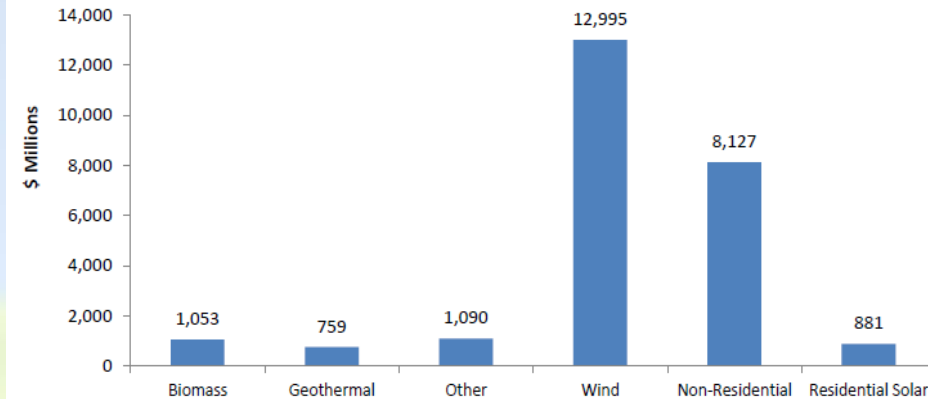


Figure 2: Awards by Project Type



- As of Sept. 30, 2012 cut-off, 210,000 applications.
- Total of approx. \$34 billion dollars estimated.
- As of early 2015, half of applications reviewed.

# Update on Section 1603 Treasury Grant Litigation

## Principal Areas of Dispute

- Qualified property. Whether property is integral to the electricity-generating activity.
- Eligible cost basis. Whether any portion of the cost basis is allocable to a non-qualifying activity or a non-qualifying intangible asset. Direct/indirect cost capitalization issues.
- Valuation/Structural issues. Whether the purchase price represents an arm's length value, is consistent with "open market expectations," or is subject to "peculiar circumstances"; related-party costs; development fees and mark-ups; sale-leaseback arrangements; inverted lease structures.



# Update on Section 1603 Treasury Grant Litigation

## Basics of Litigating Section 1603 Treasury Grant Matters

- Jurisdiction in the Court of Federal Claims.
- Claims are based on the Tucker Act (28 U.S.C. § 1491(a)(1)).
- Statute of Limitations: 6 years from the date the claim arises.
- Open question regarding interest recovery (see 28 U.S.C. § 2516).
- Open question regarding effect of sequestration.
- United States is represented by Department of Justice.
  - Civil Division.
  - Tax Division.
- Flexible consolidation of cases with similar issues.
- Judges not bound by other judges' holdings.
- Appeals to U.S. Court of Appeals for the Federal Circuit.

# Update on Section 1603 Treasury Grant Litigation

## Running Tally of 1603 Lawsuits

- There are more than 20 lawsuits that have been filed against the US Treasury Department in the US Court of Federal Claims.
- These cases include:

ARRA Energy Co., I et al.  
Clean Fuel, LLC  
LCM Energy Solutions  
Nevada Controls, LLC  
W.E. Partners II, LLC  
Sequoia Pacific Solar I, LLC  
Alta Wind I Owner-Lessor C, et al.  
Blue Heron Properties, LLC  
RP1 Fuel Cell LLC, et al.

Windpower Partners 1993, LLC  
Vasco Winds, LLC  
California Ridge Wind Energy LLC  
Bishop Hill Energy LLC  
Fire Island Wind, LLC  
Ampersand Chowchilla Biomass, LLC  
GUSC Energy, LLC  
Genesis Solar, LLC  
MeadWestvaco Corp.  
Nippon Paper Industries USA, Co., Ltd.



# Update on Section 1603 Treasury Grant Litigation

## General Guideposts

- **Some general guideposts have developed.**
  - Jurisdiction – Court of Federal Claims & Tucker Act.
  - Nature of case – money-mandating grant case.
  - Scope of damages – no consequential damages.
  - Standard of review – *de novo*.
  - Deference to Treasury Guidance.

# Update on Section 1603 Treasury Grant Litigation

## ARRA Energy Company

- *ARRA Energy Company I et al. v. United States*, No. 10-84C.
- First case filed in Court of Federal Claims in February 2010.
- Multiple mobile solar power generating systems.
- Grants denied on basis that cost basis not established.
- Government moved to dismiss case on jurisdictional grounds.
- Court of Federal Claims issued opinion in January 2011, holding it had jurisdiction because Section 1603 is a “money-mandating source of law” under the Tucker Act.
- Case later dismissed after Government raised fraud claims.

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## LCM Energy Solutions

- *LCM Energy Solutions*, No. 12-321C.
- Treasury reduced grants for 18 solar systems on the ground that the cost basis was higher than open market expectations. Applicant sought (i) full amount of grant and (ii) consequential damages.
- Court held that Applicant is not entitled to consequential damages.
- Court stated that Section 1603 contains:

“a ‘clear standard for the payment of money *and states a precise amount of money to be paid.*’ . . . This precision cannot be ‘fairly interpreted’ as mandating payment of anything beyond the exact amount of the full amount of the grant to which a given plaintiff may be entitled, much less the highly amorphous and subjective category of consequential damages.”
- *See also Clean Fuel LLC*, No. 12-79T (same holding).



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## W.E. Partners II, LLC

- *W.E. Partners II, LLC*, No. 13-54.
- Section 1603 cases handled in same manner as tax refund suits.
- “In tax refund suits, the Court reviews claims *de novo*, and the plaintiff bears the burden of proof for each claim.”
- *Bishop Hill Energy LLC*, 14-251C: Applying *de novo* review to limit discovery of Government information and documents.
- Four effects:
  - No administrative deference. Treasury cannot rely on administrative determinations.
  - Administrative proceedings at Treasury are not relevant either to Treasury or applicants.
  - Limited discovery of Treasury and Government.
  - Case tried and decided on clean slate, and not on basis of administrative record.

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## W.E. Partners II, LLC

- *Regulatory Deference Principles.* Even though the government did not argue for deference, the Court of Federal Claims concluded that the Treasury Department's interpretation of Section 1603 in the Treasury Guidance was entitled to "considerable weight as a reasonable interpretation of the statute and reasonable limitation consistent with the intent of Congress."
- Applicants may argue same deference principles against Treasury -- Treasury Guidance generally favorable to applicants.
- Regulatory deference vs. administrative deference.

# Update on Section 1603 Treasury Grant Litigation

## Case Notes

- *W.E. Partners, II, LLC*, No. 13-54. Decided on summary judgment against applicant. Involves eligible cost basis question related to use of thermal energy in cogeneration biomass plant. Federal Circuit recently affirmed.
- *RP1 Fuel Cell LLC, et al.*, No. 13-552C. First Section 1603 case to go to trial; decided in favor of applicant. Involves qualified property question with respect to gas conditioning equipment used to treat anaerobic digester gas for fuel cell power plants. On appeal to Federal Circuit.
- *Vasco Winds, LLC*, No. 13-697C. Involves NextEra wind project. Question whether cost basis reflects “open market expectations” and related-party costs. Case settled on undisclosed terms.
- *Fire Island Wind*, No. 14-403T. Involves permit-related costs for navigational aid facility (FAA). Case recently settled.
- *Genesis Solar*, No. 15-268T. First commercial scale solar facility in litigation. Qualified property issues: Auxiliary equipment, dual-use equipment, wind fencing, groundwater wells, permitting costs, and land mitigation.



# Update on Section 1603 Treasury Grant Litigation

## Major Cases

- Two of the major cases are going to trial this year.
  - *Sequoia Pacific Solar I, LLC, et al.*, No. 13-139C.
    - Resi-solar valuation issues.
    - Fact discovery completed 10/09/15; expert discovery due 02/17/16
    - Trial not scheduled; likely later this year.
  - *Alta Wind I Owner-Lessor C, et al.*, No. 13-402T et al.
    - Sale-leaseback, valuation, intangible assets, “peculiar circumstances” at issue.
    - Three-week trial scheduled to begin on 05/09/16.

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## Sequoia Pacific Solar

- *Sequoia Pacific Solar I, LLC, et al.*, No. 13-139C.
- Sequoia Pacific submitted applications for 189 residential and commercial solar energy projects based on the purchase price paid for the projects, as supported by independent appraisals.
  - Sale-leasebacks.
- The co-plaintiff Eiger Lease Co., LLC, submitted applications with respect to 4,015 residential solar energy projects.
  - The Eiger applications involved the lease of projects in which the grants were “passed-through” to the lessee entities.
- Treasury reduced the grant awards to Sequoia Pacific based on the benchmarks that Treasury adopted for solar systems.

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## Sequoia Pacific Solar

- Complaint filed February 2013.
- Gov't. filed motion to dismiss on the basis that Complaint requests Administrative Procedure Act-like review of Treasury administrative process: “[W]hat we have is a complaint that reads to us as an APA complaint.” Court declined to dismiss.
- Sparring over discovery and confidentiality issues over course of 2 years.
  - SP’s Motion to Compel Production and Interrogatory Responses.
    - Granted in part, denied in part.
  - Gov’t’s Motion to Retain Confidentiality.
    - Granted: “The agency has persuaded the court that it has an interest in keeping confidential, for example, thresholds and benchmarks amounts and how they are calculated.”



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## Sequoia Pacific Solar

- Judge Bruggink (hearing on SP's motion to compel):

“Well, here’s about the deal ... let me see if I can articulate what I’m pondering, certainly what, what happened to the plaintiffs’ applications in fact is 100% fair game. I’m inclined to think that what the benchmarks were is fair game over time. And I’m inclined to think that when the benchmarks are higher than what the plaintiff received, it creates an automatic assumption that the development of that benchmark would be relevant for the plaintiff to hear them out. Beyond that, sort of doing an autopsy after the fact of how the Government developed its approach to this program strikes me as such a large undertaking and... and that the vast bulk of which would be irrelevant at trial that I prefer to do this probably in stages.”

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## Sequoia Pacific Solar

- October 6, 2014 Order re SP's Motion to Compel Production:
  - Gov't must produce documents sufficient to identify the Benchmark or Threshold amounts that were used by Treasury or NREL in evaluating Section 1603 applications for solar photovoltaic properties from the inception of the Section 1603 Program.
  - Where, on the date of submission of any of plaintiffs' Section 1603 applications at issue in this lawsuit, Treasury's or NREL's Benchmark or Threshold amount was, on a per-watt basis, higher than the per-watt amount upon which Treasury based the Section 1603 award with respect to that application, Defendant shall produce documents sufficient to identify how that Benchmark or Threshold amount was derived.
  - Gov't must produce all documents and information upon which Treasury or NREL relied in reviewing or evaluating plaintiffs' Section 1603 applications, including but not limited to any documents or information submitted by third parties pursuant to the Section 1603 Program that were relied upon in whole or in part for that purpose.



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## Alta Wind

- *Alta Wind I Owner-Lessor C, et al.*, No. 13-402T et al.
- 20 plaintiffs total
- Sale-leaseback transactions involving wind projects
- \$226 million in grant funds at issue
- First case filed in June 2013; later consolidated with other Alta Wind cases
- Underlying dispute in the case is focused on the proper cost basis for the wind energy property for grant purposes. Treasury claims “peculiar circumstances” with respect to sale-leaseback transactions
- Plaintiffs filed summary judgment motion on grounds that purchase price paid in sale-leaseback transactions was determinative
- Gov’t filed request to stay summary judgment motions until completion of discovery
- Court granted Gov’t request and stayed proceedings pending completion of discovery. Court held that Gov’t entitled to full discovery



# Update on Section 1603 Treasury Grant Litigation

## Alta Wind

- There are four main points in the Court's analysis.

### *First:*

- The parties agreed that as a general rule the buyer's cost basis is equal to the property's purchase price. Likewise, it was undisputed that this general rule is not applicable "if the transaction in question was 'not conducted at arm's-length by two economically self-interested parties' or was based upon '**peculiar circumstances**' that contributed to a price inflated above the property's fair market value," citing *Lemmen v. Comm'r*, 77 T.C. 1326, 1347-48 (1981).
- The Court further suggested that a sale-leaseback transaction may qualify as "peculiar circumstances."
- The Court noted that "*a sale-leaseback agreement's potential for value transfers across transactions mirrors the value shifts found in Lemmen, where the US Tax Court found 'peculiar circumstances' were present.*"
- The Court agreed with the government that the sale-leaseback transaction "provides the opportunity to adjust terms to yield a higher purchase price without lowering the buyer's targeted return on investment."

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## Alta Wind

### *Second:*

- The Court observed that even if no “peculiar circumstances” exist, “the Court cannot apply the general rule for determining cost basis unless the purchase price comprises only eligible assets. In accordance with the Recovery Act, Treasury issues cash grants to applicants only for their grant-eligible property, denoted as ‘specified energy property.’”
- Because the court found that it was unclear whether the plaintiffs purchased *only* eligible property, the court determined full discovery was permitted on that basis alone.
- This discovery would include the plaintiffs’ detailed work papers, accounting records and calculations used in developing its cost schedules.
- The Court was not persuaded that discovery was not appropriate on the basis that Treasury had an opportunity to look into cost basis and was provided more than 10,000 pages in supporting documentation.
- The Court stated: “In short, a claim of this size demands that both parties have access to the underlying calculations to ensure that the Court considers the correct valuations.”



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## Alta Wind

*Third:*

- The Court agreed with the government with respect to its entitlement to discovery of the applicants' appraisals.
- The Court stated:
  - “The facts strongly suggest that the appraisal values dictated purchase price amounts, as some purchase prices are exactly equal to the appraised values. Indeed, stilted appraisal methods that comport with other evidence of value shifting would engender a genuine issue of material fact, and this precludes a grant of summary judgment.”
  - “Due to the fact that Plaintiffs considered the appraisal results in allocating the purchase price among the acquired assets, discovery of the appraisal methodology and conclusions also is necessary.”



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## Alta Wind

### *Fourth:*

- The Court agreed with the Gov't that any existing goodwill or going concern values must be subtracted from the purchase price because those items are not qualifying under Section 1603. The Court agreed that the Gov't must have full discovery to identify the amount of the purchase price that constitutes goodwill and going concern value.
  - Any existing goodwill or going concern values must be subtracted from the purchase price, as neither of these qualifies as eligible property.
  - The total purchase price cannot serve as the cost basis where Treasury Regulation § 1.1060-1 requires an allocation of an amount of the purchase price to goodwill and going concern value.
  - This determination requires consideration of “all the facts and circumstances surrounding the transaction.”

# Update on Section 1603 Treasury Grant Litigation

## Alta Wind

- Complaint filed June 2013.
- Sparring over discovery and timing.
  - Gov't Motion for Enlargement of Time to Complete Discovery.
    - “Plaintiffs’ requests were incredibly broad and sought a great deal of information that is irrelevant to the Court’s determination of the issues in this *de novo* proceeding.”
    - Granted in part, denied in part.
  - AW’s Motion to Compel Production of Documents.
    - Treasury communications withheld under deliberative process privilege. Privilege log.
    - Apr. 2, 2015 Deposition of Edward Settle; Apr. 15, 2015 Deposition of Judson Jaffe.
    - Court granted motion with respect to final pre-award documents; denied motion with respect to draft pre-award documents and non-final deliberations at Treasury.
  - Feb. 8, 2016 opinion permitting Government to file counterclaims.

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