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509 Sherbrooke Street
Commerce Twp., MI 48382
Business: 248-520-2474
Fax: 248-232-8908

Depreciation of Solar Energy Property in MACRS

Businesses rely on policy certainty to make long-term investment decisions. Depreciation is one aspect of the tax code that facilitates greater investment in renewable energy and ultimately lower costs for consumers.

MACRS as a Method of Depreciation

The Modified Accelerated Cost Recovery System (MACRS), is a method of depreciation in which a business' investments in certain tangible property are recovered, for tax purposes, over a specified time period through annual deductions. MACRS is the method of depreciation used for most property, though assets vary by class, which determines the depreciable life, or cost recovery period, of the property. Class depreciation timeframes vary between three and 50 years, depending on the certain type of property.

Qualifying solar energy equipment is eligible for a cost recovery period of five years. For equipment on which an Investment Tax Credit (ITC), the owner must reduce the project's depreciable basis by one-half the value of the 30% ITC. This means the owner is able to deduct 85 percent of his or her tax basis.

Bonus Depreciation

Congress took action to further incentivize capital investment by accelerating the depreciation schedule economy-wide. Under bonus depreciation, in the first year of service, companies could elect to depreciate 50% (in years 2015 -2017) of the basis while the remaining 50% (in years 2015 – 2017) is depreciated under the normal MACRS recovery period. In December 2015, Congress passed the Protecting Americans from Tax Hikes Act of 2015, which included a 5-year extension of bonus depreciation, including a phase-out that is structured as follows: 2015-2017: 50% bonus depreciation; 2018: 40%; 2019: 30%, 2020 and beyond: 0%.

THE SOLAR INVESTMENT TAX CREDIT

The Solar Investment Tax Credit (ITC) is currently a 30 percent federal tax credit claimed against the tax liability of commercial and utility (under Internal Revenue Code Section 48) investors in solar energy property. The business that installs, develops and/or finances the project claims the credit.

The ITC is a dollar-for-dollar reduction in the income taxes that company claiming the credit would otherwise pay the federal government. The ITC is based on the amount of investment in solar property. The commercial ITC is equal to 30 percent of the basis that is invested in eligible property which have commence construction through 2019. The ITC then steps down to 26 percent in 2020 and 22 percent in 2021. After 2023, the commercial and utility credit will drop to a permanent 10 percent. Commercial and utility projects which have commenced construction before December 31, 2021 may still qualify for the 30, 26 or 22 percent ITC if they are placed in service before December 31, 2023. The Treasury and IRS are currently drafting guidance which will inform solar developers of which percentage of ITC they will qualify for depending on when they started their project.

Page 2