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RE: Updated Guidance Relating to the Renewable Energy Technologies Income Tax Credit

The purpose of this Tax Information Release (TIR) is to update and restate the Department of Taxation's (Department) guidance regarding the Renewable Energy Technologies Income Tax Credit (RETITC) provided under Hawaii Revised Statutes section 235-12.5. This TIR supersedes TIR Nos. 2007-02, 2010-02, 2010-03, and 2012-01.

A. Who May Claim the Credit

Only the economic owner of the photovoltaic (PV) system may claim the credit. The "economic owner" of the system need not be the owner of the property being served by the system.

The determination of who is the economic owner of a system is made at the time the system is installed and placed in service. The economic owner of a system is determined with reference to the facts and circumstances of the particular transaction. Although no single test will resolve the question of who the economic owner of the system is in every situation, the following general rules will be applied by the department when analyzing a transaction:

- In the situation of leasing the system or a sale-leaseback of the system, the determination of the taxpayer who is entitled to the credit requires an analysis of whether the transaction is, in fact, a lease or sale-leaseback for federal income tax purposes. The characterization of a transaction involving a system as a sale, lease, or sale-leaseback for federal income tax purposes determines who is the economic owner of the property and thereby entitled to the tax benefits associated with the system.
- If a transaction is a lease for federal income tax purposes, the lessor is the economic owner of the system. On the other hand, if the parties characterize a transaction as a lease, but it is in reality a sale for federal income tax purposes, the lessee is the economic owner of the system.
- If a transaction is a sale-leaseback for federal income tax purposes, the buyer/lessor entering into a sale-leaseback arrangement with respect to the system is the economic owner of the system.
- If a transaction is a sale for federal income tax purposes, the buyer is the economic owner of the system, even if title to the system passes to the buyer after the system is technically installed and placed in service by the seller, but only if the system is installed and placed in service at the direction of the buyer.

Example 1:

A developer on a speculative basis (meaning that the developer has not been contracted to build the home for any specific person) plans to build and sell 50 homes, which are intended to be used as single-family residences. The developer plans to install and place in service a PV system on each of the residences during the construction of the homes. The developer is eligible to claim the credit, all other requirements for the credit being satisfied, if the developer purchases the system and installs and places it in service. The initial homeowner who then buys one of the residences from the developer will not be eligible to claim the credit, as that homeowner was not the economic owner of the system at the time the system was installed and placed in service.

Example 2:

A homeowner contracts for the purchase and installation of a PV system on their single-family residence. Because the installation and placing in service is contemporaneous with the purchase of the system being installed, the contractor would not be eligible to claim the credit even if the contractor originally purchased the system and then installed it and placed it in service prior to the passing of the title to the system from the contractor to the homeowner. The homeowner, being the economic owner of the system, would be the proper taxpayer to claim the credit.

Example 3:

The owner of a hotel purchases a PV system for installation and use in the hotel. Immediately upon installation of the system in the hotel, taxpayer acquires the system pursuant to a sale-leaseback agreement with the hotel owner. Then the taxpayer leases the system back to the hotel as required for recognition of the transaction as a valid sale-leaseback transaction for federal income tax purposes. The taxpayer, not the hotel owner, will be considered the economic owner of the system when the system was installed and placed in service; and is therefore eligible to claim the credit.

B. Repairs, Maintenance, and Additions

The previous guidance as to when repairs, maintenance, and additions would qualify for the RETITC was necessary based on the previous method of calculating the RETITC but is no longer necessary under the current “total output capacity” method of calculation. As such, the Departments previous guidance on repairs, maintenance, and additions should no longer be relied upon.

The total output capacity method of calculating the RETITC is based on the output capacity (maximum power) of the equipment that is installed and placed in service.¹ The total output capacity calculation does not consider whether a renewable energy technology system was previously installed on the property. Therefore, the total output capacity calculation should be performed without considering any previous installations regardless of whether the RETITC was claimed for the previous installations.

¹ Definition of “Installed and placed service,” Hawaii Administrative Rules (HAR) §18-235-12.5-01.

Example 4:

Taxpayer has an existing PV system that was installed and placed in service in 2015. Part of the 2015 PV system is malfunctioning and will be removed to make space for a 2020 PV system. The RETITC for the PV system installed in 2020 is not reduced because the existence of the 2015 PV system does not impact the total output capacity calculation for the PV system installed and placed in service in 2020.

Example 5:

A taxpayer has an existing PV system that was installed and placed in service in 2016. Two of the ten PV panels need to be replaced. The taxpayer is eligible to claim the cost of the two new PV panels as well as the cost to install them in the year the new panels are installed and placed into service.

Example 6:

A taxpayer has an existing 10 panel PV system. In a subsequent year, the taxpayer adds 10 additional PV panels and related equipment to the existing system. Taxpayer is eligible to claim the RETITC for the 10 additional PV panels and related equipment in the year it is installed and placed into service.

C. Accessories

“Actual cost” is defined to include the costs related to the renewable energy technology system itself, installation, and accessories.² In order for an “accessory” to be eligible for the RETITC, it must meet the following two requirements:

1. Capture a renewable source of energy, convert the renewable source of energy³, or store the converted energy; and
2. Be installed and placed in service on the same “property”⁴ in the same taxable year that a renewable energy technology system that qualifies for the RETITC is installed and placed in service.

Requirement 1: Capture, Convert or Store

Equipment that produces, consumes, or otherwise distributes the converted energy fail the first requirement and are not “accessories” that qualify for the RETITC. Items such as electric vehicle chargers and back-up gas generators are not “accessories” that qualify for the RETITC.

However, taxpayers may claim the RETITC for any portion of an installation that qualifies as a renewable energy technology system, meaning that it captures and converts a renewable source of energy. Common examples of installations that partially qualify are solar fans, solar air conditioning, and solar stoves with output capacities based on their use of PV panels for capturing sunlight and converting it into usable energy. If an installation partially

² Hawaii Revised Statutes §235-12.5(c).

³ The “accessory” must convert a renewable source of energy into a usable source of thermal or mechanical energy, electricity, or fuel.

⁴ Definition of “Property,” HAR §18-235-12.5-01.

qualifies for the RETITC, only costs attributable to the qualifying portion is considered “actual cost” that qualifies for the RETITC.

If the cost of the qualifying portion is not easily determinable, taxpayers may use a reasonable method of allocation. One reasonable method of allocation would be to deduct the value of the non-qualifying equipment.

Example 7:

The taxpayer has an existing PV system that was installed and placed in service in 2015. In 2020, the system’s inverter is malfunctioning and is replaced with a new one at a cost of \$3,000. This cost does not qualify for the RETITC because it does not meet requirement 1 and has a total output capacity of zero.

Example 8:

Taxpayers installs and places in service a solar powered stove for a cost of \$2,000. A comparable electric stove costs \$1,000. After deducting \$1,000 for the stove that does not qualify, the actual cost that qualifies for the RETITC is \$1,000.

**Requirement 2: Installed and Placed in Service on the Same “Property”
and in the Same Taxable Year**

As stated above, to be eligible for the credit, an accessory must be installed and placed in service on the same “property” and in the same taxable year as a renewable energy technology system that qualifies for the RETITC.

Example 9:

Taxpayer installs a PV system that qualifies for the RETITC and at the same time installs a PV system battery. Both installations occur on the same “property.” The battery qualifies for the RETITC as an “accessory” subject to the total output capacity calculation.

Example 10:

Assume the same facts as Example 9, except that the PV system is installed in February and the PV system battery was installed in June of the same taxable year. The battery qualifies for the RETITC as an “accessory” subject to the total output capacity calculation because it was installed and placed in service in the same taxable year as the PV system that qualifies for the RETITC.

Example 11:

Assume the same facts as Example 9, except that the PV system battery was installed and placed in service in January of the following taxable year. The battery does not qualify for the RETITC because it was not installed and placed in service in the same taxable year as a renewable energy technology system that qualifies for the RETITC.

Calculating the RETITC for Qualifying Accessories

If an accessory qualifies for the RETITC as an “accessory,” the actual cost of the accessory is added to the actual cost of the renewable energy technology system.

PV System Batteries

The Department continues to receive inquiries regarding the eligibility of PV system batteries. PV system batteries meet the first requirement because they store converted solar energy. Thus, the cost of a PV system battery will be eligible for the RETITC if it is installed and placed in service on the same property and in the same taxable year that a PV system that qualifies for the RETITC is installed and placed in service.

Example 12:

Taxpayer installs and places in service a PV system on a single-family residential property that has an output capacity (maximum power) of 3 kilowatts and an actual cost of \$20,000. Taxpayer also installs a PV system battery on the same “property” in the same taxable year that has an actual cost of \$10,000. The actual cost that is eligible for the RETITC is \$30,000. Since the total output capacity of the PV system is only 3 kilowatts, the installation only qualifies for one single-family residential credit. The RETITC for this installation is \$5,000 because 35% of \$30,000 exceeds the \$5,000 cap per system for single-family residential installations.

D. Multiple Installations During a Taxable Year

The total output capacity method of calculating the RETITC is based on the output capacity (maximum power) of all equipment that is installed and placed in service during a taxable year on a single “property.”

Example 13:

During March of 2020, Taxpayer installs and places into service a PV system consisting of 10 photovoltaic panels, each of which has an output capacity (maximum power) of 0.250 kilowatts on a single-family residential property. During August of 2020, Taxpayer installs and places into service another PV system consisting of 10 photovoltaic panels, each of which also has an output capacity (maximum power) of 0.250 kilowatts on the same the single-family residential property. The total output capacity of both installations is 5 kilowatts because the output capacity of both installations must be combined. Since each single-family residential system must have a total output capacity of at least 5 kilowatts, one system has been installed and placed into service for the purpose of calculating the RETITC.

Example 14:

Assume the same facts as Example 12, except that Taxpayer starts a third installation of another PV system consisting of 10 photovoltaic panels, each of which also has an output capacity (maximum power) of 0.250 kilowatts on the same the single-family residential property in December of 2020, but the installation is not completed until January of 2021. Because the December installation was not installed and placed in service until 2021, the total output capacity calculation will not include the December installation. However, the December installation shall be included in the calculation of the total output capacity for the 2021 RETITC.

E. Installed and Placed in Service

A renewable energy technology system is installed and placed in service when it is ready and available for its specific use.⁵ Systems installed for residential property will be deemed to be installed and placed in service when the actual cost has been incurred; all installation, including all related electrical work, has been completed; and any required requests for inspection of the installation has been received by the appropriate government agency.⁶ However, if the residential installation fails to pass all the required inspections the credit is properly claimed in the taxable year in which the system passes such inspection.

All renewable energy technology systems that are not for residential or mixed-use property are deemed to be for commercial property. The commercial property category covers a broad range of installations that have different regulatory requirements and necessary approvals. “Ready and available for its specific use” in the context of the commercial property category means that all permits have been secured and the renewable energy technology system can be activated, as validated by a licensed professional engineer.

It is important to note that this analysis focuses on whether the system could have been turned on, not whether it was actually turned on.

Example 15:

Assume the same facts as Example 14, except that Taxpayer activates the renewable energy technology system on December 31, 2020, but doesn’t submit a request for inspection until January 4, 2021. Activating the system does not change the date that the system was installed and placed in service, Taxpayer shall claim the RETITC for the December installation in the 2021 tax year.

F. EFFECTIVE DATE

This TIR is effective immediately and applies to any system placed in service prior to its effective date where the statute of limitations for assessment remains open.

For additional information regarding this TIR, please call the Technical Section at (808) 587-1577.

/s/

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HRS Sections Explained: HRS §235-12.5

HAR Sections Explained: HAR §§18-235-12.5-01 to 18-235-12.5-06

⁵ Definition of “Installed and placed service,” HAR §18-235-12.5-01.

⁶ *Id.*