Hodgson Russ LLP ATTORNEYS

NEW YORK APPELLATE COURT DECISION STOPS SHORT OF SETTLING SOLAR PROPERTY TAX ISSUES

Hodgson Russ Renewable Energy Alert
September 22, 2020

Both renewable energy market participants and taxing jurisdictions in New York State have long been bedeviled by inconsistent and unclear real property tax policy and assessments. A recent decision from the State's appellate court could have helped clarify the confusion, but stopped short of doing so.

In *Cornell Univ. v. Bd. of Assessment Review and Shana Jo Hilton, as Assessor of the Town of Seneca, New York*, 186 A.D.3d 990 (4th Dep't 2020), a case in which Cornell contended that a solar facility developed on its land was personal property, not real, and therefore not taxable, the Fourth Department Appellate Court instead held that solar energy systems are properly classified as taxable real property. The decision did not, as some in New York's solar market hoped it might, address how such systems should be assessed or whether different components of the solar facility should be treated differently – that is, whether the solar panels themselves, which the Internal Revenue Service has categorized as removable, personal property,[1] are real property, or whether only the racking and portions affixed to the ground should be designated as such. The Fourth Department also did not address an issue raised by the lower court – that an individual municipality that prohibits permanent affixing of the system to the ground by mandating decommissioning cannot declare that equipment to be permanent real property. Thus, uncertainty still reigns.

Background

The underlying litigation arose when Cornell University ("Cornell") brought a proceeding under Real Property Tax Law Article 7 challenging the Town of Seneca's taxable assessment of a solar energy system that was owned by a third-party, Argos Solar, LLC ("Argos"), who was not a party to the litigation.

As all solar systems do, this one consisted of solar panels, wires, a racking system, inverters, poles or pilings, a control system, and a concrete pad on which the equipment sat. The system was described by the developer as designed for disassembly and removal at the end of the contract term. All that was required for removal was unbolting and unplugging the panels, disassembly of the racks, and carting the equipment away. Following disassembly and removal, the equipment could be reused.

Attorneys

Joseph Endres
Michael Hecker
Elizabeth Holden
Charles Malcomb
Paul Meosky
Aaron Saykin
Daniel Spitzer
Jeffrey Stravino
Brianne Szopinski
William Turkovich
Sujata Yalamanchili
John Zak
Henry Zomerfeld

Practices & Industries

College & University
Real Property Tax Assessment & Eminent Domain
Tax-Exempt Organizations

Cornell offered two primary arguments why the system was not taxable: (1) that Cornell is a tax-exempt educational institution; and (2) that the system constitutes personal property, not real property. In response, the Town of Seneca (the "Town") contended that (i) although Cornell is tax-exempt, the system was owned by Argos, a for-profit entity, and (ii) that the system met the definition of "real property" because it was intended to be permanently affixed to the ground. The lower court had rejected the Town's arguments and held the System was not taxable, primarily finding that the system should be deemed effectively owned by Cornell, a non-profit, and thus tax exempt. In dicta, the Court also noted the inconsistency between a town requiring a solar system to be removed and taxing it as a permanent fixture.

The Appeal

On appeal, the Town prevailed in its argument that the system was a fixture and therefore was real property. The Town also contended that Cornell's tax-exempt status did not prohibit taxation of the system because it is owned by Argos and not Cornell. As to the first issue, the appeals court held that the system is a fixture under both the Real Property Tax Law and common law, and therefore subject to real property taxation. Without addressing the potentially different status of the various components of the system, the Court held that the System is a fixture as defined by Real Property Tax Law § 102 (12)(b), which provides that real property includes "[b]uildings and other articles and structures, substructures and superstructures erected upon, under or above the land, or affixed thereto."

Furthermore, the Court held that the system met all three elements of the common law fixtures test – annexation, adaptation, and intention. The system consisted of "nearly 1,600 piles driven directly into the ground and nearly 400 piles set on footings of concrete." The system and associated equipment were attached by nuts and bolts and installed on a concrete slab. Collectively, the manner in which the System was installed, the court held, confirmed that it was "annexed to the real property."

The Court also held that the second element of the common law fixtures test was met insofar as the system applied to the use and purpose of the land, which was dedicated to generating solar energy as part of the sustainability efforts and educational mission of Cornell.

Finally, the Court held that the third element of the test was met because the power purchase agreement between Cornell and Argos demonstrated that they desired and intended the system to be permanent for the term of the agreement. Notably, the removable nature of the system was not only required by the agreement, but was a condition of the Town Planning Board approval of the system installation at Cornell.

Cornell's Tax-Exempt Status Does Not Change the Analysis

While there was no dispute that Cornell is a tax-exempt educational institution, the Court reasoned that its exempt status did not impact its determination that the system constituted taxable real property. The agreement between Cornell and Argos separated ownership of the land from that of the system, and Argos is responsible for removal of the system and all taxes associated with ownership of it. Cornell has the option of purchasing the system at the end of the term of the agreement. Therefore, Cornell lacks the necessary level of "dominion and control" over the System to exempt the System from taxation.

Hodgson Russ Insights

The Court's holding in this case unfortunately does not improve the current New York state of affairs with respect to real property taxation of renewable energy installations. Cornell has filed for re-argument and leave to appeal to the New York State Court of Appeals, but the primary issues facing the industry are unlikely to be resolved there.

While most assessors are using the income capitalization approach, an effort to confirm that methodology as appropriate for renewable energy systems did not survive the last budget process, nor did an effort at centralizing determination of capitalization rates. Thus some assessors are still pushing the cost methodology despite it being disfavored by the courts. And numerous assessors are including intangible assets like environmental attributes in the income capitalization approach even though these are not real property income streams under New York law.

The limitations of this holding only further highlight the need for the legislature to bring certainty to the assessment of renewable energy projects. Unless the legislature either enacts a law that classifies components of a system as personal property or the State establishes a required PILOT amount or assessment methodology that fairly values the real property components of renewable energy and storage systems, taxing jurisdictions will continue to assess projects ad hoc. Furthermore, legislative action addressing the methodology for determining the taxable value of these projects will bring much needed clarity to project developers and municipalities alike, potentially avoiding protracted litigation.

If you have any questions about the tax assessments and exemptions related to renewable energy projects or other properties, please contact Daniel Spitzer (716.848.1420), Noah Shaw (518.736.2924), or a member of our Renewable Energy Practice. If you received this alert from a third party or from visiting our website, and would like to be added to our Renewable Energy mailing lists or any other of our mailing lists, please visit us at: https://forms.hodgsonruss.net/sign-up-for-email-and-other-communications..html.

[1] 26 CFR § 1.856-10(g); Internal Revenue Bulletin: 2016-29, *Example 8* ("The Treasury Department and the IRS have concluded that PV modules and inverters that are used in the generation of energy for sale to third parties do not qualify as [inherently permanent structures]…").