FORTIFIED SOLAR

Investment Tax Credit (ITC) Recapture Risks and Fortified Solar’s Mitigation Strategies

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Overview

The Investment Tax Credit (ITC) offers substantial benefits for investors in renewable energy, but it also comes with compliance requirements that extend over a five-year recapture period. If certain conditions are not met—such as ownership continuity, qualified use, or operational status—the IRS may “recapture” part or all of the credit previously claimed.

Fortified Solar (FS) has developed a comprehensive risk management framework to protect Solar Facility Owners (SFOs) from ITC recapture by combining conservative legal structuring, professional tax advisory support, and practical operational safeguards.

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1. Ownership Change During the 5-Year Recapture Period

Risk: Selling, transferring, or disposing of a solar facility before the five-year holding period can trigger ITC recapture under IRC §48.

Mitigation: FS requires all SFOs to maintain ownership of their facility for at least five years. If liquidity is needed, Eclipse Financing (a wholly owned FS subsidiary) can purchase the facility for the loan balance plus accrued interest after the five-year mark—providing a compliant and orderly exit option.

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2. Foreclosure During the Recapture Period

Risk: A foreclosure for lack of payment, will cause a loss of ITC eligibility.

Mitigation: FS structures its loan agreements with a “tolling provision” that prevents a default from triggering during the five-year recapture window. If lease or loan payments are delayed, interest accrues without creating a taxable default event.

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3. Project Ineligibility or Non-Qualifying Property

Risk: The IRS may deny ITC eligibility if a system fails to meet technical qualifications under IRC §48 or supporting regulations.

Mitigation: FS has engaged **legal and accounting professionals**, to validate that all projects qualify as "energy property." Each project includes legal and technical memoranda confirming compliance with IRC §48, cost-basis determination, and proper "placed in service" documentation.

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4. Passive Activity or Material Participation Challenge

Risk: If an investor's participation is deemed passive under IRC §469, tax credits may be limited to passive income, or credits may be disallowed.

Mitigation: For investors looking for active income offsets, FS recommends each investor own their system through a single-member LLC and track activity through the **Tax Credit Institute Portal**. This platform maintains a participation log consistent with legal and accounting guidance on material participation thresholds and documentation standards.

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5. Over-Leverage or "At-Risk" Rule Violation

Risk: If an investor's ownership structure does not satisfy the IRS "at-risk" rules under IRC §465, the ITC may be disallowed or partially recaptured.

Mitigation: Each SFO single-member LLC is the borrower of record and the owner of the solar facility. The financing provided by Eclipse Financing is structured to ensure the entity itself—not the individual investor—is at risk for its invested capital, satisfying the IRS "at-risk" requirement while protecting the investor from personal liability.

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6. IRS Audit or Substantiation Risk

Risk: Inadequate recordkeeping can result in disallowed credits during an IRS audit.

Mitigation: FS maintains a centralized **Tax Credit Institute portal** that stores all supporting documentation—construction photos, engineering certifications, legal memoranda, and agreements—ensuring immediate access and full audit readiness.

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7. Improper Exit or Donation Timing

Risk: Disposing of or donating the system before five years can trigger partial recapture of the ITC.

Mitigation: FS recommends holding the facility for at least five years before any sale or donation. After year five , investors may choose to **donate** their solar asset to a 501(c)(3) organization, converting it into a charitable deduction while remaining fully compliant. They have also worked with legal and tax professional on other exits to minimize audit risk.

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8. Nonqualified Debt and "Phantom Income" Risk

Risk: If the financing used to purchase the solar facility is not considered qualified debt under IRS rules, the IRS could reduce or disallow the ITC. Additionally, nonqualified or forgiven debt can create phantom income—taxable income recognized without any actual cash received.

Mitigation: Fortified Solar structures each investment so that the SFO's single-member LLC is the borrower and owner of the solar facility. Financing through Eclipse Financing is secured by the asset and documented with standard repayment terms, ensuring the debt is qualified and at-risk. This preserves the full ITC and prevents phantom income recognition.

Conclusion

Fortified Solar's proactive compliance framework provides comprehensive risk mitigation for ITC recapture risk—ownership continuity, operational stability, and substantiation. Through expert tax advisory partnerships, flexible asset management, and conservative structuring, FS safeguards investors' credits while maintaining alignment with IRS guidelines. The result: investors enjoy the full financial benefit of the ITC with minimized exposure to recapture events.