

CLIENT ALERT

Recent Case on Use of Development Fees: *California Ridge Wind Energy LLC v. United States*, Nos. 2019-1463, 2019-1465 (Fed. Cir. May 21, 2020)

JUNE 3, 2020

The Federal Circuit Appeals Court has released its [opinion](#) on its May 21, 2020 decision to affirm the decisions in the California Ridge Court of Claims cases, which found that the use of certain development fees was a sham to increase improperly the amount on which the taxpayers could claim an ARRA Section 1603 Cash Grant.

The Appeals Court noted:

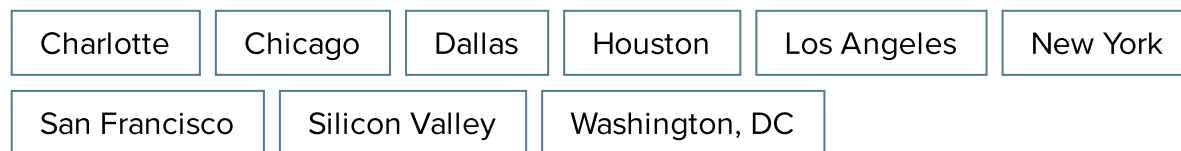
“We read the Court of Federal Claims opinion as finding that the amounts stated in the development agreements do not reliably indicate the development costs. That finding is not clearly erroneous. It is sufficiently supported by at least the round-trip nature of the payments; the absence in the agreements of any meaningful description of the development services to be provided; and the fact that all, or nearly all, of the development services had been completed by the time the agreements were executed.”

The same reasoning and concerns could be applicable in the case of development fees paid in the context of the ITC. Concern about these cases and the issues they address has been ongoing for some time. In situations where development fees are used, development fee agreements should be entered into prior to the performance of any services, and the nature and timing of such services should be described in detail. Such agreements should include only reasonable, market-based compensation, for services actually to be provided by the developer. Maintaining careful documentation about the timing and completion of the covered services, as well as a market-based third-party appraisal of the value of the services provided, could provide important supporting evidence in the event an IRS challenge. In addition, any arrangement that involves “round tripping” of money, or other situations that might call into question the economic substance of the development fee agreement, should be avoided. Because the use of development fees has generated unfavorable scrutiny, taxpayers may wish to consider transaction structures that avoid the use of development fees, although any such alternative structures should take into account the general issues raised in this case, such as the need for market-based economics and increased scrutiny of related-party transactions and “round-tripping” of money.

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