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Tax Legal Update

American Recovery and Reinvestment Act of 2009: Renewable Energy Incentives for Business

One month after the inauguration of President Obama, Congress passed the "American Recovery and Reinvestment Act" (the "Stimulus Act") in an effort to save and create jobs, stimulate growth in the economy, and provide substantial funds to transform the country's energy capability, address climate change, and reduce dependence on foreign oil.

The Stimulus Act promotes clean, efficient energy projects; enhances renewable energy production; and builds upon the state's existing "green building" requirement by providing funds for the renovation of public buildings. The act provides $30 billion for initiatives such as a new "Smart Grid," expected to modernize the nation's electricity grid to make it more efficient and reliable. It also provides $20 billion in tax incentives for renewable energy and energy efficiency over the next 10 years and institutes a three-year extension of the production tax credit for electricity generated by wind (through 2012) and from biomass, geothermal, hydropower, landfill gas, waste-to-energy, and marine facilities (through 2013). The act offers additional grants of up to 30 percent of the cost of building a new energy facility to address prevailing renewable energy market concerns.

The incentives in the act provide enhanced benefits to energy users who generate power for their own use and for sale into the grid. Moreover, for the first time, targeted federal tax credits are available to encourage the development of a domestic manufacturing industry to support the renewable energy industry.

The Stimulus Act provides a substantial supplement to the state funds historically available for alternative or renewable energy development, including funds available under Project 150 from the Connecticut Clean Energy Fund. The combination of the funds and tax incentives provided under the Stimulus Act and funding under existing state renewable energy investment programs greatly enhances Connecticut's ability to meet its goal to increase the amount of energy available from Class I renewable sources to 20 percent by 2020. Governor Rell has stated that 25 percent of all state and local projects funded by stimulus dollars will be used for "green" projects.

Following are some of the key energy-related tax incentives provided under the Stimulus Act.

Current Tax Incentives for Renewable Energy (IRC §§ 45 and 48)

Under current law IRC § 45, the energy production tax credit, provides a credit based on kilowatt hours for electricity generated from qualified energy resources at qualified facilities generating power for the use of unrelated third parties. The qualified renewable energy resources and facilities are:

- Wind
- Closed-loop biomass (organic material)
- Open-loop biomass (agricultural livestock and solid wood waste material)
- Geothermal energy
- Solar energy
- Small irrigation power

- Municipal solid waste
- Qualified hydropower production
- Marine and hydrokinetic renewable energy

Also, under current law IRC § 48, the energy credit, provides for a 30 percent credit through 2016 for the cost of tangible personal property used in the generation of power through solar or fuel cell applications and a 10 percent credit for microturbine power.

Stimulus Act Extends Section 45 Credit

In a development that provides greater certainty for energy producers and project developers, the Stimulus Act extends the availability of the section 45 credit for three years through 2013 for qualified facilities other than wind and marine and hydrokinetic renewable energy resources. For wind facilities, the extension runs through 2012, and for marine and hydrokinetic facilities, a two-year extension brings the placed-in-service date to the last day of 2013. A technical correction clarifies that small irrigation power facilities are included in marine and hydrokinetic renewable energy facilities as of October 3, 2008, the effective rate of the Energy Improvement and Extension Act of 2008.

Act Makes Section 48 Credit Available to Section 45 Energy Sources

In a major change that greatly increases the attractiveness of the renewable energy credit, the act permits a taxpayer who places section 45 facilities in service during 2009 through 2013 to elect the 30 percent business energy expenditure credit of section 48 in lieu of the section 45 credit based on generation of electricity. This provides an added incentive for renewable energy projects in a preproduction stage by capturing a benefit for upfront costs in advance of production.

Solar energy and fuel cell technology are not included in the property eligible for this election because they are already eligible for the section 48 expenditure credit. Wind energy property is eligible only if placed in service during 2009 through 2012. Refined coal and Indian coal facilities that are included in section 45 are not eligible for this election.

A taxpayer electing under this provision is not permitted to take the section 45 generation credit with respect to any property to which the election pertains. In addition, property subject to the election is subject to the section 48 tax basis reduction rules when financed by subsidized energy financing or industrial development bonds unless it is constructed, reconstructed, or erected after December 31, 2008. In addition, the $4,000 credit cap on small wind energy property is eliminated for such property placed in service in 2009 and later but only to the extent of construction, reconstruction, or erection occurring after December 31, 2008.

Grants Are Now Available in Lieu of the Section 45 or 48 Credit

In a development that effectively makes the business energy credit a refundable credit of particular value to investors with insufficient current tax liability to absorb a credit, the secretary of the Treasury is authorized to make grants of 30 percent of the basis of property that is a section 45 facility or section 48 property. To be eligible, either property must be placed in service during 2009 or 2010 or construction must be begun during 2009 or 2010 and completed prior to January 1, 2013 (for wind facility property), 2014 (for other section 45 property), or 2017 (for specified energy property described in section 48). The grant is limited to 10 percent for qualified microturbine, combined heat and power, geothermal, and geothermal heat pump property. A grant under this section is not includible in income but does reduce the basis of property by 50 percent of the amount of the grant.

A grant may not be made to a governmental entity or agency or to any entity exempt from tax under section 501(a). A grant precludes the recipient from claiming a section 45 or 48 credit for the property that is the subject of the grant, and the act provides for recapture where the credit has been claimed prior to approval of the grant. Applications for grants under this provision must be received before October 1, 2011.

The Act Provides a New Credit for Advanced Energy Manufacturing Projects

The changes discussed so far focus on the creation or enhancement of the production of renewable energy. In a very significant development, the Stimulus Act provides a new credit designed to encourage the development of a domestic manufacturing base to support the renewable energy production. This new addition to the investment credit, to be codified as section 48C, provides a 30 percent credit for qualified property to be used in a qualified advanced energy manufacturing project. Such a project is one that establishes, reequips, or expands a manufacturing facility for the production of the following:

- Property used to produce energy from the sun, wind, geothermal deposits, or other renewable resources
- Fuel cells, microturbines, or an energy storage system for use with electric or hybrid-electric motor vehicles
- Electric grids to support transmission or storage of intermittent sources of renewable energy
- Property designed to capture and sequester carbon dioxide

- Property designed to refine or blend renewable fuels, other than fossil fuels, to produce energy conservation technologies, including energy-conserving lighting technologies and smart grid technologies
- New qualified plug-in electric drive motor vehicles, qualified plug-in electric vehicles, or components designed specifically for use with such vehicles, including electric motors, generators, and power control units
- Other advanced energy property designed to reduce greenhouse gas emissions, as determined by the Secretary of the Treasury

Qualifying property is depreciable property used in a qualified advanced energy project. Only tangible personal property is eligible, not buildings or their structural components. Excluded is property designed to manufacture equipment for use in refining or blending any transportation fuel other than renewable fuels. The basis of property giving rise to the credit must be reduced by the amount of the credit.

The credit must be applied for and approved and total credits as of enactment are limited to $2.3 billion appropriated for the purpose. The Secretary of the Treasury, in consultation with the Secretary of Energy, is required to establish a program by August 17, 2009, to award certification to eligible projects. Only those projects for which there is a reasonable expectation of commercial viability are to be considered, and approved projects must also provide these elements:

- Greatest domestic job creation
- Greatest net impact in avoiding or reducing air pollutants or anthropogenic emissions of greenhouse gases
- Lowest levelized cost of generated or stored energy or of measured reduction in energy consumption or greenhouse gas emission
- Shortest project time from certification to completion
- Greatest potential for technological innovation and commercial deployment

Project applications for certification must be made within two years of the act's February 17, 2009, enactment, and within one year thereafter, applicants must demonstrate that certification requirements have been met. A certified project must be placed in service within three years of certification. At the end of four years after enactment, the Secretary is directed to review credit allocations and redistribute any credits not used either because of a revoked certification or because of receipt of insufficient applications.

The Credit for Alternative Fuel Refueling Property Is Increased

In an effort to enhance the infrastructure for development of alternative forms of motor vehicle fuel, the Stimulus Act modifies the IRC section 30C credit for qualified alternative fuel vehicle refueling property by increasing the per location cap on qualified hydrogen refueling property from $30,000 to $200,000. The credit for nonhydrogen-qualified refueling property is increased from 30 percent to 50 percent and the cap on the credit for such property from $30,000 to $50,000 per location. The cap on the credit for both hydrogen and nonhydrogen-qualified alternative fuel refueling property installed on property used as a principal residence is increased from $1,000 to $2,000. These increases in credit and caps apply only to qualified property placed in service during calendar years 2009 and 2010.

The Credit Cap and Basis Reduction for Subsidized Energy Financing of Small Wind Property Is Repealed

The act eliminates from IRC section 48 the $4,000 tax credit cap for small wind energy property and repeals the requirement that the basis of such property be reduced where it is the subject of subsidized energy financing, including industrial development bonds.

The Act Makes Other Changes Related to Energy

The act also provides a tax credit for carbon dioxide sequestration and for increases in the amounts available for issuance of Clean Renewable Energy Bonds and Qualified Energy Conservation Bonds. For additional information on both types of bonds, please click here. Also amended are provisions primarily of interest to consumers: the Nonbusiness Homeowners Energy Credit (IRC § 25C) is extended to 2010 and substantially modified; the cap on Residential Energy Efficient Property (IRC§ 25D) is eliminated; the IRC section 30D plug-in vehicle credit is modified, and two new credits relating to plug-in technology are created.

Summary

The alternative energy tax incentives provided under the Stimulus Act, together with other funding for alternative energy development, present opportunities for businesses and government to invest in energy projects that will both enhance growth in our economy and move us in the direction to cleaner energy sources and energy independence. If you have questions regarding the tax incentives available under the act, you may speak to any of the following members of our Tax Group:

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