



Tax Credit Alert

Recent developments in tax credits

A publication of Nixon Peabody LLP

JANUARY 27, 2009

Energy-related proposals in the House and Senate, as of January 27, 2009

By Forrest David Milder

In this *Tax Credit Alert*, we'll discuss the proposals that have gotten traction in the renewable energy area, especially Congressman Rangel's proposal in the House and Senator Baucus's markup in the Senate. President Obama made renewables a cornerstone of his campaign, and we expect to see some significant changes in this marketplace. Of course, what appears below is based largely on our reading of pending legislation and reports from the relevant House and Senate committees through January 27, 2009; **it could all change at any time**. We know from years of following tax legislation that even a proposal that is in both House and Senate versions of a bill might ultimately be removed from the final legislation, or it might be changed in a small way that has a large impact on a particular deal. So, plan your affairs with care, and be sure to check with us before assuming that any provision will wind up becoming law.

As of January 27, 2009, here's what we're seeing in the proposals.

1. **PTC extension.** Both the House and Senate would provide a three-year extension for most production tax credits (PTCs). For wind, this means placement in service before January 1, 2013, and for biomass, geothermal, landfill gas, trash, and qualified hydro, this means placement in service before January 1, 2014. Marine and hydrokinetic renewables would get a two year extension, and therefore the placement in service deadline would also be prior to January 1, 2014. Senator Grassley (lead Republican on the Senate Finance Committee) has said that he would make this extension five years or permanent.
2. **Claiming ETC instead of PTC.** Both would allow a project owner to claim the 30-percent energy tax credit (ETC) for what would otherwise be many (but not all) PTC-eligible investments for 2009 and 2010. This proposal could have far reaching implications—the ETC is claimed all at once and is subject to recapture for five years, while the PTC is claimed over 10 years and does not have a recapture rule. As written, this would make it possible for an owner of a wind, geothermal, or other PTC-eligible facility to lease it to others and still claim the credit, and it would also make these facilities qualify for the 90-day sale leaseback

and lease-pass-through rules. Development fees and other capital expenditures associated with investment tax credits would also generate new interest.

3. **DOE grants.** Probably the most significant of the possible changes is the House proposal to provide many project owners with a choice – they can elect to receive a 30-percent Department of Energy *grant* instead of most PTCs or ETCs for 2009 and 2010. The grant would only be 10 percent for a handful of less-favored ETC facilities—certain geothermal, microturbine, and combined heat and power projects – and coal and irrigation projects would not be eligible at all. The grant would not be taxable, but the taxpayer’s basis in the property would be reduced by half the amount of the grant (like the ETC it replaces), and the grant would be subject to possible five-year repayment on disposition of the project, similar to the 5-year recapture rule that applies to the ETC. Grants are required to be provided “within 60 days of the application.” The Senate proposal does not have DOE grants..”
4. **Subsidized energy financing.** Both proposals eliminate the basis reductions for subsidized energy financing and private activity bonds on ETC transactions. There is no comparable provision for the PTC, but, presumably, a wind or other PTC project could elect ETC treatment (if eligible), and then also take advantage of this new bond exemption.
5. **Technical proposals.** The Senate proposal would allow all 10 years of the PTC to be used against the alternative minimum tax, and a five-year carryback on tax credits. Grassley would make this 10 years. The House would keep the current one-year carryback. The Senate proposal would also allow tax credits carried to or from 2008 and 2009 to be used against 100 percent of income. As of now, the Senate proposals, which do not necessarily allow TARP recipients to carry back *losses*, do not have a similar limitation on their ability to carry back *credits*.
6. **CREBs and conservation bonds.** Both proposals add an additional \$1.6 billion in CREBs (Clean Energy Renewable Bonds). These apply to public and cooperative power projects that are not eligible for PTCs. The proposed legislation would also authorize \$2.4 billion of energy conservation bonds for state and local projects to curb greenhouse gas emissions.
7. **Manufacturing and research credits.** The Senate would also add a new, 30-percent investment tax credit for investment in “qualified property” used in a “qualified advanced energy manufacturing project,” up to a national total of \$2 billion. The project must re-quip, expand, or establish a facility that manufactures (i) property that produces energy from the sun, wind, or geothermal; (ii) fuel cells, microturbines, or energy storage systems for electric or hybrid vehicles; (iii) electric grids for renewable energy; or (iv) equipment for use in carbon capture and sequestration. Both the House and Senate would add a new, 20-percent credit for qualified research expenses paid or incurred in 2009 or 2010 for renewable energy, energy conservation, efficient transmission and distribution of electricity, and carbon capture and sequestration
8. **Non-commercial residential energy.** Both would lift the dollar caps (ranging from \$500 to \$2,000) on the 30-percent investment tax credits for non-commercial, residential “small wind,” solar water heater and geothermal heat pump expenditures. Note that the 2008 Act already repealed what had been the \$2,000 cap on residential solar electricity. Additional expansions of other residential energy savings measures are also included.

Other important proposals

Although not included in the most recent energy legislation, we wanted to highlight two other relevant proposals:

1. **Bonus depreciation**—reinstates 50-percent Bonus Depreciation for property placed in service in 2009, and for certain property with a longer depreciable life, for property placed in service in 2010.
2. **NOLs of acquired banks**—eliminates the ability of an acquiring bank to use an acquired bank's loss carryforwards (IRS Notice 2008-83). This proposal is intended to draw banks back into the tax-credit marketplace, and get them to use tax-favored investments, rather than the acquisition of failed banks with large-loss carryforwards, as a way to reduce their tax liability.

As noted at the beginning, these proposals are being modified and augmented constantly, and there can be no assurance that any particular provision won't be completely eliminated or merely changed, sometimes in a way that is truly hard to appreciate until it is actually applied to a particular fact pattern. Please feel free to contact Forrest Milder (617-345-1055, fmilder@nixonpeabody.com) or Jim Duffy (617-345-1129, jduffy@nixonpeabody.com) with your thoughts and questions.

IRS Circular 230 notice: Any tax advice contained herein was not intended or written to be used, and cannot be used, by you or any other person (i) in promoting, marketing, or recommending any transaction, plan, or arrangement or (ii) for the purpose of avoiding penalties that may be imposed under federal tax law.