



Tax Credit Alert

Recent developments in tax credits

A publication of Nixon Peabody LLP

FEBRUARY 18, 2009

Renewable energy tax provisions in the American Recovery and Reinvestment Act of 2009

By *Forrest David Milder*

This *Tax Credit Alert* describes the provisions of the American Recovery and Reinvestment Act of 2009 (2009 Act) that relate to the Section 45 Production Tax Credit (PTC) and the Section 48 Energy Tax Credit (Energy Tax Credit), as well as a new program that allows project owners to get grants from the federal government, rather than offer the credits to investors, and several other new provisions of interest. Those who read our January 27 “snapshot” of the bill that ultimately became the 2009 Act will recognize most of these newly enacted provisions.

Extension of the Production Tax Credit. The 2009 Act provides a full, three-year extension for many PTC-eligible facilities: wind projects will now qualify for the credit if they are placed in service by December 31, 2012, and biomass, geothermal, landfill gas, and trash will now qualify for the credit if they are placed in service by December 31, 2013. Finally, the placed-in-service date for qualified hydropower and marine and hydrokinetic facilities was extended by two years, also to December 31, 2013.

Claiming the Energy Tax Credit for a PTC facility. The 2009 Act adds a new subsection to Section 48 allowing a wide range of PTC-eligible facilities to claim the 30-percent Energy Tax Credit, rather than the production tax credit. These include wind, biomass, geothermal, landfill gas, trash, qualified hydropower, and marine and hydrokinetic facilities placed in service from 2009 through 2012 (for wind) and through 2013 (for the other power sources). Projects making the election are no longer eligible for the PTC. The Act does not provide any guidance as to how or when the election is made, although the Conference Report indicates that only property eligible for five-year depreciation can qualify under this rule. Obviously, this is a big change—in particular, if these PTC facilities make the election, then they no longer need to sell electricity in order to generate the credit, and the entire 30 percent is obtained at once, rather than over 10 years. Note that geothermal now appears in both the PTC and the 10% subsection of Section 48. Presumably, a geothermal facility would choose PTC, and then elect a 30% credit under Section 48 to maximize its credit.

Converting the Energy Tax Credit to a Grant. Facilities eligible for the energy tax credit can instead claim a dollar-for-dollar grant from the US Treasury. Eligible facilities include both those that have always been eligible for energy credits—in particular, solar and fuel cell projects, as well as the new PTC-eligible facilities that elect Section 48 treatment. Most facilities are eligible for a 30-percent

grant, but some (qualified microturbine, combined heat and power, and geothermal heat pump) qualify only for a smaller, 10-percent grant. Because geothermal now appears in both the PTC and the 10% subsection of Section 48, we'd expect a geothermal facility to choose PTC, elect a 30% credit, and then claim a 30% grant.

The Act provides some strict timetables. First, construction of the project must begin in 2009 or 2010; second, the Treasury must pay the amount of the grant within 60 days of the placed-in-service date or the date of the application, if later; third, the project must be placed in service by the PTC or Energy Credit deadline that otherwise applies to the particular facility. And there are technical rules as well: the grant is not income, and expenditures made with the grant are included in basis and eligible for depreciation, but reduced by half the amount of the grant (i.e., like the adjustment that applies to the credit; effectively, 85 percent of costs paid with a grant will be eligible for depreciation). Treasury is authorized to provide recapture rules which would presumably be similar to the five-year, 20-percent per year rule that generally applies to investment tax credits. Facilities owned by federal, state, or local governments or tax-exempt entities (including partnerships or LLCs which have these entities as partners or members) cannot claim grants.

Subsidized energy financing. The 2009 Act repeals the rule that reduces the amount of the Section 48 energy credit if a project benefits from below-market financing or tax-exempt debt.

Bonus depreciation. The Act reinstates 50-percent bonus depreciation for property placed in service in 2009,

Bonds. The Act increases the authorized amount of Clean Renewable Energy Bonds (CREBs) that benefit state, local, and tribal governments; public power providers; and cooperatives, by \$1.6 billion, and the authorized amount of qualified energy conservation bonds for state, municipal, and tribal government programs, as well as utility programs that provide energy-efficient property to rate-payers, by \$2.4 billion. These and other bond changes will be covered in greater detail in another NP *Client Alert*.

Miscellaneous changes. For small wind facilities placed in service after December 31, 2008, the \$4,000 cap on the credit is eliminated. The 2009 Act also eliminates the caps on the 30-percent credit for many non-business energy properties, including solar water heaters, small wind facilities, and geothermal heat pumps. (You'll remember that 2008 legislation had already eliminated the cap on solar electric.) The 2009 Act extends the placed-in-service date for many non-business energy efficiency improvements to December 31, 2010; increases the credit rate for those expenditures from 10 percent to 30 percent; and sets a single overall (and lifetime) cap for these expenditures at \$1,500, rather than the several smaller caps for each kind of improvement in effect under prior law. The 2009 Act sets many new rules for alternative fuel vehicles and their refueling and also for electric drive vehicles. Finally, the Act provides a new, 30-percent credit for investment in a "qualifying advanced energy manufacturing project" that re-equips, expands, or establishes a manufacturing facility for a wide variety of renewable technologies.

As you can see, the changes made by the 2009 Act are extensive, and will lead to major changes in the way that renewable transactions are structured. Furthermore, some of the credit changes described above only apply to the portion of expenditures incurred after 2008. As a result, it can be important to talk to us to determine the application of transition rules.

Please feel free to contact your regular Nixon Peabody attorneys, or Forrest Milder (617-345-1055, fmilder@nixonpeabody.com), Jim Duffy (617-345-0000, jduffy@nixonpeabody.com), Herb Stevens (202-000-0000, hstevens@nixonpeabody.com), or Michael Goldman (202-000-0000, mgoldman@nixonpeabody.com) with your thoughts and questions. We look forward to hearing from you.