THOMPSON HINE

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ENERGY & TAX UPDATE

Congress Passes Extensions for Renewable Energy Tax Incentives

Just when hope seemed lost that the members of Congress would be able to reconcile their differences prior to the presidential election, the Energy Improvement and Extension Act of 2008 (the "Act") was signed into law on October 3, 2008, as part of H.R. 1424, the vehicle for the economic rescue legislation. The Act amends the Internal Revenue Code to provide incentives for energy production and conservation by extending and expanding certain expiring investment and production tax credits and providing for new tax credit bonds. This bulletin focuses on the renewable energy incentives of the Act. Further bulletins will expand on the energy efficiency and carbon mitigation provisions.

PRODUCTION TAX CREDIT EXTENSION

Section 101 of the Act extends the renewable energy Production Tax Credit (PTC) placed-in-service date for wind and refined coal facilities by one year, until January 1, 2010. Refined coal is a liquid, gaseous or solid fuel produced from coal in a way that results in reduced emissions of nitrogen oxide and either sulfur dioxide or mercury.

The placed-in-service date for the PTC for other types of facilities, such as open- and closed-loop biomass, geothermal, solar, small irrigation power, landfill gas, trash and qualified hydropower, is extended for two years, until January 1, 2011. The PTC for biomass is broadened to include expansions of existing facpilities that occur after October 3, 2008 (the date of enactment), but only to the extent of the increased amount of electricity produced by the facility because of the new biomass unit.

The Act further expands the PTC to include marine and hydrokinetic renewable energy facilities placed in service prior to January 1, 2012. The Act defines "marine and hydrokinetic renewable energy" as energy derived from waves, tides and currents in oceans, estuaries and tidal areas; free-flowing water in rivers, lakes and streams; free-flowing water in an irrigation system, canal or other man-made channel; and differentials in ocean temperature (ocean thermal energy conversion). Energy that is derived from any source using a dam or other diversionary structure is not included in the term. To qualify, marine and hydrokinetic facilities must have a nameplate capacity rating of at least 150 kilowatts.

Section 101(f)(1) of the Act provides that the effective date for the PTC extensions, except as otherwise provided, applies to property originally placed in service after December 31, 2008.

Energy Credit Extension

Section 103 of the Act extends the energy credit termination date for solar energy, fuel cell and microturbine property until January 1, 2017. The Act also permits the energy credit to be used against the alternative minimum tax. Section 103(d) of the Act increases the credit limit for fuel cell property from $500 to $1,500.

The Act expands the energy credit to include a credit for combined heat and power system property (CHP) that is placed in service prior to January 1, 2017. The Act defines CHP as property comprising a system that uses the same energy source for the simultaneous and sequential generation of electrical power, mechanical shaft power, or both, in combination with the generation of steam or other forms of useful thermal energy, and that produces at least 20 percent of its total useful energy as thermal energy not used to produce electrical or mechanical power and at least 20 percent of its total useful energy as electrical or mechanical power (or combination thereof). Such a system must have an energy efficiency percentage[1] of greater than 60 percent. A qualified facility cannot exceed a capacity of 50 megawatts or have a mechanical energy capacity in excess of 67,000 horsepower.

Qualified small wind energy property also now qualifies for the energy credit. A "qualifying small wind turbine" is defined under the Act as a wind turbine with a nameplate capacity of less than 100 kilowatts. This tax credit applies to small wind energy property until December 31, 2016.

Clean Renewable Energy Bonds

Section 107 of the Act makes New Clean Renewable Energy Bonds (New CREBs) available for capital expenditures by governmental bodies, public power providers or cooperative electric companies for qualified renewable energy facilities. First created by the Energy Policy Act of 2005, a CREB is a special type of bond, known as a "tax credit bond," that offers issuers the equivalent of an interest-free loan for financing qualified energy projects for a limited term. Unlike a conventional bond, where the bond issuer pays interest to the bondholder, a CREB-holder receives a tax credit that may be used to offset both income and alternative minimum taxes in lieu of interest.

New CREBs deliver an incentive comparable to the PTC; however New CREBs operate as a financing tool, whereas PTC benefits are received only after the facility is financed and electricity is generated. The goal of New CREBs is to provide municipal utilities, rural electric cooperatives and other public power entities a subsidy to invest in renewable energy generation. This is demonstrated by the fact that, in contrast with the treatment of CREBs (the provisions of which were also extended to cover bonds issued until December 31, 2009), the tax credit generated by New CREBs is not required to be recognized as income in the taxpayer's gross income for the year. Renewable energy facilities eligible for New CREB financing include all types of PTC-qualified facilities, except for refined coal. Under Section 107(a) of the Act, the national New CREB limitation is $800 million, of which a third will be allocated to each type of qualified institution respectively. Further, Section 107(a) provides that New CREB status is available for obligations issued after October 3, 2008, and prior to December 31, 2009.

FOR MORE INFORMATION

We will continue to monitor and keep clients informed of new legislative and regulatory developments regarding renewable energy tax incentives. If you have questions or would like more information, please contact:

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[1] Energy efficiency percentage is calculated as the ratio of the total useful electrical, thermal and mechanical power produced by the system at normal operating rates divided by the lower heating value of the fuel sources for the system.