



# Support for Renewable Energy Programs Gaining Momentum

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It's been more than a year and half since President George W. Bush signed the Energy Policy Act of 2005 (P.L. 109-58) into law. Since that date, the discussion surrounding the need for renewable energy resources has escalated dramatically. The popularity of hybrid automobiles, the war in Iraq, countless newspaper articles focusing on the global warming debate and Al Gore at the Academy Awards are just a few slices of anecdotal evidence the alternative energy discussion has now officially gone mainstream.

The Energy Policy Act represented a successful first step by Congress to pass a comprehensive energy package in an effort to execute on a national energy strategy proposed four years earlier. The act established \$14.5 billion in tax incentives over a 10-year period to encourage, among other things, the continued expansion and use of alternative energy sources such as solar, wind, biomass and others.

The shot in the arm that this legislation gave to the production tax credit (PTC) under Internal Revenue Code (IRC) Section 45 (wind, biomass etc.) and the investment tax credit (ITC) under IRC Section 48 (solar etc.) energy has proved to be significant. Energy projects determined to not be financially feasible by developers in the past have become feasible. Large institutional players that had been investing their capital in housing tax credits and elsewhere became more open to the idea of alternative energy investments as they searched for alternative tax credit investments providing greater returns. What this simply means is that more alternative energy facilities will be developed. As one might expect, the PTC and ITC incentives are predicted to have a significant impact on our environment and economy, as well as create attractive investment opportunities for developers and tax credit investors.

The immediate impact these subsidies have had is not lost on the current Congress, which to its credit, has acted quickly and was able to get the PTC and the ITC subsidies extended through December 31, 2008 (2006 Tax Relief and Health Care Act (H.R. 6111)). The December 31, 2008 expiration date is where we currently stand. On the table, however, is another bill that proposes to extend the ITC subsidies for solar and fuel cell property through December 31.

## **Federal and State Agency Incentives**

Global demand for energy continues to soar due to rapid growth in population while sources of fossil fuels continue to diminish and become more precarious and difficult to obtain. The Senate Committee on Energy and Natural Resources responded to the aforementioned situation with the 2005 Energy Policy Act. With that bill, the Energy Committee made progress in improving energy supplies, boosting energy conservation and developing the new energy technologies needed for the future. Various state agencies have supplemented the federal incentives with a variety of their own incentive and rebate programs. For example, the California Public Utilities Commission has created the Self-Generation Incentive Program (SGIP) and the California Solar Initiative. The New Jersey Board of Public Utilities has created the New Jersey Clean Energy Project and Florida recently passed its own energy act to establish rebates and other incentives.

At the federal level, the 2005 Energy Policy Act created or increased tax incentives in the form of the Section 45 production tax credit and the Section 48 investment tax credit. (See sidebar on page 3.) Typically, a wind farm development delivers tax benefits to the investor in the form of federal production tax credits, accelerated depreciation deductions and cash flows from energy sales. The typical photovoltaic (solar) installation delivers tax benefits to the investor in the form of federal investments tax credits (energy credits), accelerated depreciation deductions and cash flows from state rebates (as applicable) and energy sales.

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Solar and wind transactions are proving to be appealing investment alternatives for institutional investors that historically have invested in low-income housing tax credit (LIHTC) transactions. The desire for investment diversification coupled with potentially higher yields appear to have made solar and wind investment funds look attractive when compared to those delivered by LIHTC investment funds in recent years. But as was the case with the LIHTC program, until the program was extended indefinitely under then President Clinton in 1993, institutional capital for alternative energy programs won't likely truly commit until it sees evidence the programs are here to stay and not subject to continued short term renewals by Congress.

The Securing America's Energy Independence Act (H.R. 550 and S. 590) introduced in by Reps. Mike McNulty, D-N.Y., and Dave Camp, R-Mich., and Sens. Gordon Smith, R-Ore., and Ken Salazar, D-Colo., would extend solar investment tax credit incentives, discussed herein, through December 31, 2016. This legislation also proposes a three-year accelerated depreciation period for all solar equipment eligible for the business solar tax credits.

"It is imperative that this Congress be bold and push energy tax policies that will encourage and speed the development of our nation's renewable resources," Salazar said February 27 in a statement about the proposals.

Other Senate sponsors of S. 590 are: Sens. Olympia Snowe, R-Maine, Robert Menendez, D-N.J., Richard Lugar, R-Ind., John Kerry, D-Mass., Edward Kennedy, D-Mass., Wayne Allard, R-Colo., Ron Wyden, D-Ore., Joseph Lieberman, D-Conn., Frank Lautenberg, D-N.J., Maria Cantwell, D-Wash., and Mary Landrieu, D-La.

Even though current proposals call for a long term extension for the solar ITC incentives, many believe a long term extension of the tax credit incentives for wind, solar and other renewable energy sources is critical. An extended program would create stable market conditions that would help resolve the equipment procurement issues now being faced by solar and wind developers alike. In addition the cost of wind, solar, and other renewable energy equipment and property would be reduced as "panic" demand is reduced, energy equipment companies have time to efficiently increase their production and new equipment manufacturers are able to enter and establish themselves in the market place. Further, an extended initiative would likely help stimulate increased private investment in research and development activities to develop state of the art energy technologies. Last but not least the Solar Energy Industries Association estimates tax credits from the extension bills could fuel creation of 55,000 solar industry jobs by 2016, and "encourage states to invest billions of dollars in renewable energy infrastructure," said Rhone Resch, SEIA president.

All of the above topics and more will be presented at Novogradac & Company LLP's Financing Renewable Energy Conference: Using Tax Credits to Finance Solar, Wind and Other Renewable Sources, on May 2-3, 2007 at the Fairmont Hotel in San Francisco, Calif. ❖

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## **IRC §45: Electricity produced from certain renewable resources**

IRC Section 45 provides owners or operators of certain electricity generating facilities a renewable electricity production tax credit to produce electricity from “qualified energy sources.” Energy sources that qualify include wind, biomass, geothermal, solar, irrigation, solid waste and hydropower. Currently, the production tax credit is 1.9 cents for each kilowatt hour (adjusted annually for inflation by the Internal Revenue Service) of electricity produced by a “qualified facility” that is sold to an unrelated party during the tax year. The production tax credit runs for 10 years, beginning on the date the facility is placed in service, and is reduced if the producing facility is financed with grants, tax-exempt bonds, subsidized energy financing or other credits. In the case of facilities with more than one person having an ownership interest, the production from the facility shall be allocated among the owners in proportion to their respective ownership interests in the gross sales from the facility to the extent allowed by the IRC and the regulations thereunder.

## **IRC §48: Energy credit**

IRC Section 48 provides owners of certain energy property an investment tax credit equal to 30 percent of the basis of each energy property placed in service during the tax year. Property eligible for the 30 percent investment tax credit includes equipment that uses solar energy to generate electricity to heat or cool a structure, equipment that uses solar energy to illuminate the inside of a structure using fiber-optic distributed sunlight, and qualified fuel cell property. Energy property that does not fall under the aforementioned types of energy property qualifies for a 10 percent energy investment tax credit. This energy investment tax credit generally does not apply to the portion of the basis of any energy property that is attributable to qualified rehabilitation expenditures (IRC Section 47) and is generally reduced if the energy property is financed with subsidized energy financing or private activity bonds (IRC Section 146 Volume Cap Bonds-Tax Exempt).

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