

# Beyond Government Tax Credits: Prospects For Reaching Policy Goals

Federal incentives have proven invaluable, but the U.S. solar policy landscape presents several questions.

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Historically, the U.S. federal government has provided support for solar energy by incenting solar development with a combination of grants, loan guarantees and tax credits. The American Recovery and Reinvestment Act of 2009 (ARRA) provided additional and improved benefits, but they are subject to time limitations.

These incentives work in concert with state-level policies supporting solar energy, which have typically taken the form of regulatory measures such as state-level renewable portfolio standards (RPS).

Federal policy, however, may soon include a renewable electricity standard (RES) and carbon emissions caps. The form of traditional federal incentives is also likely to change.

A number of proposals are now in the works. The House has passed H.R.2454, the American Clean Energy and Security Act of 2009 (ACESA), which is a comprehensive energy bill that includes a cap-and-trade component and a national RES.

S.1462, the American Clean Energy Leadership Act of 2009 (ACELA), which also includes a national RES, earned bipartisan support and approval from the Senate Energy and Natural Resources Committee. A majority of senators on the Senate



*PROINSO is supplying Mecasolar trackers for this 1 MW PV project in California's Madera Water District. Photo courtesy of PROINSO.*

Environment and Public Works Committee also voted to move S.1733, the Clean Energy Jobs and American Power Act (Kerry-Boxer), to the Senate floor with a cap-and-trade component.

Although these bills have yet to be enacted into law, they present a number of new policies, programs and ideas that will affect the development of solar energy projects. In addition to legislation, a host of regulatory changes can also be expected as a consequence of the Environmental Protection Agency's formal designation of carbon dioxide as a pollutant in April 2009.

As we progress through the first months of 2010, the debate in Washington continues on a number of issues, as climate and energy are taken up by Congress - in addition to health care, financial industry reform and, especially in the face of midterm elections this fall, job creation and economic recovery.

Despite the many challenges, President Obama remains committed to a federal energy policy that includes a combination of incentives (often known as "carrots") and regulatory measures (often known as "sticks").

In his State of the Union address on Jan. 27, Obama insisted that "to create more...clean energy jobs, we need more production, more efficiency [and] more incentives," and emphasized that "passing a comprehensive energy and climate bill" is needed "to make clean energy the profitable kind of energy in America."

## Program modifications

Tax credits have long been at the center of federal incentives for solar energy. The form of the tax incentive for solar changed in February 2009, when ARRA Section 1603 modified the tax credit for solar by requiring that the Treasury Department provide cash grants to applicants who place in service renewable energy fa-

cilities that would otherwise qualify for the investment tax credit (ITC). Congressional committees are currently considering modifying and expanding the grant program.

Washington policy-makers have generally looked favorably upon the grant program, which awarded approximately \$2.3 billion to over 240 applicants in its first six months. (The program rules were promulgated in July.) The current discussion is whether and how the program might be extended. A simple fix would be to extend the date for commencement of project construction to the end of 2011 or 2012.

One proposal being pursued by congressional staff is to convert the grant program into a refundable ITC. The rules that have been applicable with respect to grants would be maintained (for example, the more liberal recapture rules, the use of blockers to cure ownership by otherwise disqualified entities and the refund being made to the project instead of to taxpayers).

There may be additional benefits, such as eliminating the start-date limitation and having disqualified ownership result in proportional - as opposed to complete - disallowance.

Because the refundable ITC would be tied to a tax filing, the process for receiving it would be the same as filing for the ITC, rather than the separate regime currently in place for the Section 1603 grant.

This change means that refunds under the new program would be paid considerably later, after the annual tax return is filed for the year in which the project is completed. Refunds would also be subject to offset if the taxpayer has unpaid taxes or debts due to the government. It is also anticipated that refunds of \$2 million or more will be subject to a higher level of scrutiny.

Bonus depreciation - permitting a taxpayer to deduct 50% of the basis of an asset in the first year - expired at the end of 2009. Bonus depreci-

ation is thought to provide an incentive to investment by permitting a significant amount of business investment to be expensed in the first year and is, therefore, viewed as economically stimulative.

The extension of bonus depreciation enjoys a broad base of political support, and the extension of bonus depreciation last year was of limited use to solar energy facilities simply because so few went into service.

### **Pending bills**

Another tax credit of significant benefit to the solar market established by ARRA is the Section 48C advanced energy manufacturing tax credit. On Jan. 8, the Treasury announced 182 awardees (out of more than 500 applicants) for a total of \$2.3 billion in tax credits.

For this round, CaliSolar, First Solar, Nanosolar, Solarworld, Suntech, SunPower and many other well-known solar firms received tax credits, following the competitive solicitation process. The many disappointed applicants are now pressing for additional allocation. Fortunately, Treasury Secretary Timothy Geithner announced on Jan. 28 that Obama's budget will contain \$5 billion more in credits.

The best possibility for changes to the tax benefits related to solar is likely to be the jobs bill that the Senate Finance Committee is to consider, or a tax cleanup bill that was scheduled to be passed by the end of February. As with any legislative action, anything and everything is subject to change.

The Title XVII loan-guarantee program received a boost from ARRA, with its expansion under Section 1705 to include commercialized technologies and the appropriation of \$6 billion to underwrite credit subsidy costs (i.e., the premium required to be paid for the loan guarantee).

The program has been subject to a fair amount of criticism regarding its cost and complexity, and a number of statutory requirements restrict the

Department of Energy's (DOE) flexibility with respect to the issuance of guarantees.

For example, projects with Section 1705 loan guarantees must commence construction by the end of September 2011. Several larger projects in the West will have difficulty meeting this date, given the National Environmental Policy Act (NEPA) compliance requirement, delays in permitting and the substantial transmission network upgrades necessary to accommodate those projects.

Additionally, the program suffered a setback in 2009, when \$2 billion of its funding was removed to fund the expansion of the Cash for Clunkers automobile-exchange program.

Although the DOE's ability to issue additional solicitations under Section 1705 is restricted until additional funding for credit subsidy costs is appropriated, Obama's budget proposal contains additional funds for this top-priority program.

The program itself is subject to statutory revision. Both ACESA and ACELA would establish a Clean Energy Deployment Administration (CEDA) to succeed the current Title XVII federal loan-guarantee program.

Both of these bills contemplate that CEDA could provide a variety of financial products, including direct loans, guarantees, letters of credit and secondary-market support. Furthermore, both bills emphasize support of breakthrough technology and provide for issuance by the Treasury of bonds in amounts of up to \$7.5 billion to \$10 billion to fund CEDA, depending on the bill.

However, the House bill contemplates CEDA as an independent corporation, while the Senate version establishes CEDA within the DOE. The House bill requires a finding that insufficient commercial lending is available for the technology as a condition to CEDA support; the Senate version does not have such a limitation.

The list of ideal potential changes to the loan-guarantee program for

improved usefulness in the development of solar energy projects is lengthy. Positive changes would include the extension or elimination of the construction commencement date, simplification of the application process, streamlining NEPA compliance and eliminating the need for credit ratings.

In general, the solar sector has been supportive of a larger federal financing program for renewables, with a preference for a well-capitalized financing corporation outside of the DOE, without the emphasis on breakthrough technologies or the requirement that private commercial financing be absent.

Any short-term solution to the federal loan-guarantee program's issues, such as the redirection of the Cash for Clunkers funding, is likely to occur in the proposed jobs bill. Extension of the required construction commencement date and other fixes to the loan-guarantee program appear to have an uncertain future at this point, and they may be overtaken by the larger proposals for CEDA.

CEDA, meanwhile, is most likely to be undertaken as part of a broader energy bill. Although ACESA and ACELA were early entrants in the race for a comprehensive energy bill (including cap-and-trade mechanisms, in the case of ACES), the common view today is that climate legislation is not likely to arrive this year.

A scaled-back energy bill like ACELA might be more viable, but the challenge of any scaled-back bill is the ability to generate enough votes as particular benefits are stripped away. A bill favoring only renewable energy, for example, could face stiff opposition from the natural-gas or coal industries. ACESA, on the other hand, is a massive bill covering topics dear to a host of constituents.

Renewable energy groups have been pushing for a national RES for years. ACESA would establish a national RES with a target of 20% renewables by 2020, while ACELA

would require 15% by 2021. In each case, energy efficiency can meet a large portion of the requirement - up to 40%, in certain circumstances, under ACESA.

The bills provide for an alternative compliance penalty of \$25/MWh in the case of ACESA, or \$21/MWh, in the case of ACELA. The bills provide a three-times multiplier for renewable energy credits from distributed generation, which is a major incentive for distributed-generation solar projects.

In general, solar stakeholders have been supportive of proposals for a national RES, but they tend to favor a strong mandate (25% by 2025), a separate mandate for energy efficiency, a 5 MW maximum size on distributed generation systems and an alternative compliance penalty of at least \$50/MWh.

The prospects for a national RES this year are murky, because the RES would most likely need to arrive through a larger energy bill. Moreover, opposition to the RES can be expected from regions that, thus far, have been slow to adopt state-level RPS programs, as well as from the fossil-fuel industries.

Those industries have good reason to be concerned about the effect of a national RES, considering the effect on new contracts for generation in states with a high RPS, such as California. Business interests generally do not favor any mandated purchasing program that might increase costs.

Furthermore, the RES may also be seen as a poor substitute for cap-and-trade, and it may not engender support from the environmental community outside of renewable energy manufacturers and developers. Indeed, an argument can be made that RES may be unnecessary if a robust cap-and-trade regime is enacted.

A distant cousin of the RES is a national feed-in tariff. Although feed-in tariffs have been adopted in a handful of jurisdictions in the U.S., they are generally limited to smaller

projects. California policy-makers are currently considering a program that incorporates generation projects up to 20 MW - an increase from the current 3 MW statutory program.

A national feed-in tariff was considered a non-starter as late as 2008, but it seems to have gained credence as an alternative means of supporting renewables. Note, however, that none of the major proposed energy bills includes a national feed-in tariff.

Assuming a national RES is enacted, then a related question is whether there is a need for the tax credits or the Treasury grant program beyond the immediate stimulus period. Because the purpose of the credits is to help underwrite the costs of renewable energy in competition with other technologies, an RES precludes the competition and, hence, obviates the need for the subsidy.

This argument makes renewable energy proponents nervous, inasmuch as the bid prices in the RES would then be higher, without the hidden subsidy of the credit or grant programs. Notwithstanding renewable energy proponents' concerns, one should expect that a phase-out of the credit and grant programs would likely result from a national RES.

Although climate-change legislation made significant progress in both the House and the Senate in 2009, recent political developments suggest that current proposals are unlikely to move forward - at least in their current form.

For instance, Sen. Scott Brown, R-Mass., made opposition to carbon legislation one major aspect of his successful campaign for the Senate seat vacated by the late Edward Kennedy, and Senate Democrats no longer hold the 60 votes required by Senate rules to block a Republican filibuster.

Moreover, the cap-and-trade component of ACESA and Kerry-Boxer (ACESA's Senate counterpart with respect to climate issues) has come under attack from both sides of the political spectrum. On one side are those who argue that cap-and-

trade is too expensive or too risky, given the current economic climate.

On the other side of the opposition are some environmentalists, who praise the proposal to reduce carbon to 83% below 2005 levels by 2050, but claim that the proposed legislation is too generous to carbon emitters, especially in the electricity sector, and have gone so far as to oppose ACESA as a consequence.

Finally, transmission issues that have yet to be resolved at the federal level continue to pose problems for large-scale solar projects. In particular, multi-state transmission lines and upgrades are required to fully develop the vast solar resources located in the Southwest.

Cooperation and planning among the states has been difficult, given the tendency to favor local voting interests over broader regional objectives. Federalization of transmission planning and siting remains at the center of the renewable energy industry's agenda. Both ACESA and ACELA provide some guidelines for regional transmission planning under the

Federal Energy Regulatory Commission's auspices. Federal siting authority would be available for interstate transmission projects after the failure of the affected states to take action - at least in the West under ACESA.

Cost allocation of multi-state transmission lines presents a complicated political problem that is made even more difficult by the current economic climate and budgetary constraints. Additionally, decreased congestion on transmission lines brought on by the recession may make additional transmission build-out a harder sell for regulators charged with protecting consumers from rate increases.

Jurisdictional turf wars between state regulatory agencies (and federal regulators) can be expected. Furthermore, political pressure to develop in-state resources should also be anticipated, as job creation remains at the forefront of any political battle.

Concerns abound with respect to the consequences of creating centralized permitting with eminent-domain rights. Most observers now

believe that the best outcome we might see this year is the kind of broad directives contained in ACESA, which defers the hard issues to a year-long regulatory debate.

Overall, the drivers for legislative action in 2010 will be creating jobs, and secondly, avoiding issues that could be problematic for legislators facing a difficult election contest in November.

Hence, actions to extend the benefit of stimulus programs have a good prospect for success. Larger energy issues may be addressed in a slimmed-down version of the energy bills already proposed, but there is no certainty of passage. ☞

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