

DEPARTMENT OF TAXATION

2014 Fiscal Impact Statement

1. **Patron** Thomas K. Norment, Jr.

2. **Bill Number** SB 653

3. **Committee** Senate Finance

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

4. **Title** Renewable Energy Property; Tax Credits.

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would allow eligible taxpayers to claim a transferable credit against the individual income tax, the corporate income tax, and the insurance premiums license tax for placing renewable energy property into service in the Commonwealth during the taxable year. The tax credit would equal 40 percent of the costs paid or incurred by the taxpayer to place the property into service, not to exceed \$2.5 million for any individual piece of renewable property. Any costs related to existing infrastructure would not be eligible for the credit.

If the renewable energy property that is eligible for the credit is not in excess of \$250,000, the tax credit would be allowed for the taxable year in which the property is placed into service. For all other renewable energy property, the tax credit would be allowed in three equal taxable year installments, beginning with the taxable year in which the property is placed into service.

The tax credit under this bill would be administered by the Department of Mines, Minerals, and Energy ("DMME"). The total amount of credits that DMME could approve in any given fiscal year would be limited to \$10 million.

For purposes of this bill, "renewable energy" would be defined as energy derived from sunlight; wind; falling water; biomass, sustainable or otherwise; waste; landfill gas; municipal solid waste; wave motion; tides; or geothermal power. "Renewable energy" would not include energy derived from coal, oil, natural gas, or nuclear power. The term "renewable energy property" would mean property that produces renewable energy and related devices necessary for collecting, controlling, storing, exchanging, conditioning, or converting such energy.

This bill would be effective for taxable years beginning on or after January 1, 2014.

6. **Budget amendment necessary:** Yes.

ITEM(S): 115, Department of Mines, Minerals, and Energy

7. Fiscal Impact Estimates are: Preliminary. (See Line 8).

7a. Expenditure Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Positions</i>	<i>Fund</i>
2013-14	\$0	0	GF
2014-15	\$70,000	1	GF
2015-16	\$70,000	1	GF
2016-17	\$70,000	1	GF
2017-18	\$70,000	1	GF
2018-19	\$70,000	1	GF
2019-20	\$70,000	1	GF

8. Fiscal implications:

Administrative Costs—Department of Mines, Minerals, and Energy (“DMME”)

DMME reports that its administrative costs would include dedicating one full-time employee to manage the Renewable Energy Tax Credit program and consulting with several subject matter experts to develop the necessary guidelines and process applications within the period prescribed under this bill.

Administrative Costs—Department of Taxation

The Department of Taxation (“the Department”) has not assigned any administrative costs to this bill because the changes required by a single bill such as this can be implemented as part of the annual changes to our systems and forms. As stand-alone legislation, the Department considers implementation of this bill as “routine,” and does not require additional funding.

The Department will provide specific administrative costs on any legislation that is not “routine.” Additionally, the Department will review all state tax legislation likely to be enacted prior to the passage by each house. If the aggregate number of routine bills likely to pass either house is unusually large, it is possible that additional resources will be required. If so, the Department will identify the costs at that time.

Revenue Impact

This bill would have an unknown negative impact on General Fund revenue. The total negative revenue impact would not exceed the \$10 million cap; however, it is unclear how many taxpayers would qualify for and claim this tax credit.

This credit could be claimed for placing in service the following types of renewable energy property: solar photovoltaic systems, solar thermal systems, wind systems, hydroelectric systems, biomass systems, and geothermal systems. It is unknown how many of these systems would be placed into service during the applicable taxable years.

Energy Derived from Sunlight (Solar Photovoltaic and Solar Thermal Systems)

During 2009 and 2010, DMME administered a solar rebate program, through which it processed 351 claims for rebates. Applying data from this solar rebate program, it is

estimated that approximately \$1.73 million worth of credits for solar photovoltaic and solar thermal systems would have been issued under the tax credit program proposed by this bill. However, it is unknown if the same amount of tax credits would be issued under this bill for Taxable Year 2014 and thereafter.

Energy Derived from Wind Systems

According to the US Energy Information Administration (USEIA), very little wind energy was consumed in Virginia from 2007 to 2011. Accordingly, it is projected that the amount of credits claimed for placing wind systems into service would have a relatively small negative revenue impact.

Energy Derived from Hydroelectric (Water) Power

Hydroelectric energy is the renewable energy source that produces the most electricity in the United States. In 2012, it accounted for approximately 7 percent of total U.S. electricity generation, and approximately 56 percent of the total generation from renewable energy. According to the USEIA, Virginia currently has 21 hydroelectric power plants in operation. It is unknown how many credits would be claimed for investment in this type of renewable energy property.

Energy Derived from Biomass Systems

According to the USEIA, there are 23 biomass power plants currently located in Virginia. Although the USEIA indicates that Virginia has abundant biomass, biomass energy consumption has fallen 15 percent in the past 5 years. Accordingly, the amount of credits claimed for this type of energy would likely have a relatively small negative revenue impact.

Energy Derived from Geothermal Power

According to the USEIA, consumption of geothermal energy increased by approximately 80 percent from 2007 to 2011. However, due to the significant investment required for geothermal systems, it is unknown how much property would be placed in service that would qualify for tax credits under this bill.

9. Specific agency or political subdivisions affected:

Department of Mines, Minerals, and Energy
Department of Taxation

10. Technical amendment necessary: No.

11. Other comments:

Federal Business Energy Investment Tax Credit

Under federal law, businesses may claim a tax credit equal to 30 percent of the costs of qualified fuel cell property; equipment which uses solar energy to generate electricity, heat or cool a structure, or provide solar process heat; equipment which uses solar energy to illuminate the inside of a structure using fiber-optic distributed sunlight; and qualified small wind energy property.

Businesses may claim a credit equal to 10 percent of the costs of any other energy property. Other types of energy property include equipment used to produce, distribute, or use energy derived from a geothermal deposit; qualified microturbine property; combined heat and power system property; and equipment which uses the ground or ground water as a thermal energy source to heat a structure or as a thermal energy sink to cool a structure.

To qualify for the credit, the original use of the property must begin with the taxpayer, or the property must be constructed by the taxpayer. Additionally, the property must be depreciable or amortizable and the property must meet the performance and quality standards set forth in the Treasury Regulations.

No credit is allowed with respect to property for the taxable year in which a grant is made under § 1603 of the American Recovery and Reinvestment Tax Act of 2009 or any subsequent taxable year. A recapture provision applies if a credit is determined for any taxable year before which a grant is made.

For purposes of the credit, “qualified fuel cell property” is defined as a fuel cell power plant which has a nameplate capacity of at least 0.5 kilowatt of electricity using an electrochemical process and has an electricity-only generation efficiency greater than 30 percent.

“Qualified microturbine property” means a stationary microturbine power plant which has a nameplate capacity of less than 2,000 kilowatts and an electricity-only generation efficiency of not less than 26 percent at International Standard Organization conditions.

“Combined heat and power system property” is defined as property comprising a system which uses the same energy source for the simultaneous or sequential generation of electrical power, mechanical shaft power, or both, in combination with the generation of steam or other forms of useful thermal energy; which produces at least 20 percent of its useful energy in the form of thermal energy which is not used to produce electrical or mechanical power, and at least 20 percent of its total useful energy in the form of electrical or mechanical power; the energy efficiency percentage of which exceeds 60 percent; and which is placed in service before January 1, 2017.

“Qualified small wind energy property” is defined as property which uses a wind turbine that has a nameplate capacity of not more than 200 kilowatts to generate energy and is placed into service in service before January 1, 2017.

Federal Residential Energy Efficient Property Tax Credit

Under federal law, individual taxpayers may claim a nonrefundable credit equal to 30 percent of qualified solar electric property, solar water heating property, fuel cell property, small wind energy property, and geothermal heat pump property expenditures made during the taxable year. The credit cannot exceed the sum of the taxpayer’s regular tax liability less any nonrefundable personal credits, foreign tax credits, Puerto Rico and possession tax credits for the taxable year. Any unused credit may be carried over to the following taxable year and added to the residential energy efficient property credit for that

year. This credit is available for qualifying property placed in service before January 1, 2017.

For purposes of the residential energy efficient property tax credit, a “qualified solar water heating property expenditure” is defined as an expenditure for property to heat water for use in a dwelling unit located in the United States and used as a residence by the taxpayer if at least half of the energy used by the property for such purpose is derived from the sun. To qualify for the credit, solar water heating property must be certified for performance by the Solar Rating Certification Corporation or a comparable entity endorsed by the government of the State in which such property is installed.

“Qualified solar electric property expenditure” is defined as an expenditure for property which uses solar energy to generate electricity for use in a dwelling unit located in the United States and used as a residence by the taxpayer.

“Qualified fuel cell property expenditure” is defined as an expenditure for qualified fuel cell property, as defined in IRC § 48(c)(1), installed on or in connection with a dwelling unit located in the United States and used as a principal residence by the taxpayer. The credit for fuel cell property cannot exceed \$500 per half kilowatt of capacity of the qualified fuel cell property to which the expenditure relates.

“Qualified small wind energy property expenditure” is defined as an expenditure for property which uses a wind turbine to generate electricity for use in connection with a dwelling unit located in the United States and used as a residence by the taxpayer.

“Qualified geothermal heat pump property expenditure” is defined as an expenditure for any equipment which (i) uses the ground or ground water as a thermal energy source to heat a dwelling unit located in the United States and used as a residence by the taxpayer or a thermal energy sink to cool such unit, and (ii) meets the requirements of the Energy Star program.

Federal Nonbusiness Energy Property Tax Credit

Under federal law, individual taxpayers may claim a nonrefundable credit equal to 10 percent of the cost of qualified energy efficiency improvements and residential energy property expenditures made during the taxable year. There is a lifetime credit limit of \$500, less the total credits allowed to the taxpayer for all prior taxable years ending after December 31, 2005.

To qualify for the credit, the expenses incurred must be for property originally placed in service by the taxpayer prior to January 1, 2014, and made on or in connection with a dwelling unit located in the United States that is owned and used by the taxpayer as his principal residence at the time of installation.

For purposes of the nonbusiness energy property tax credit, “qualified energy efficiency improvements” are defined as any energy efficient building envelope component which meets the criteria established by the 2009 International Energy Conservation Code or Energy Star program requirements, if such component is installed in or on a dwelling unit located in the United States and used by the taxpayer as the taxpayer’s principal

residence, the original use of such component commences with the taxpayer, and such component reasonably can be expected to remain in use for at least five years.

“Building envelope component” means any insulation material or system which is specifically and primarily designed to reduce the heat or loss or gain of a dwelling unit when installed in or on such dwelling unit; exterior windows, including skylights; exterior doors; and any metal roof or asphalt roof installed on a dwelling unit, but only if such roof has appropriate pigmented coatings or cooling granules which are specifically and primarily designed to reduce the heat gain of such dwelling unit.

“Residential energy property expenditures” is defined as expenditures made by the taxpayer for qualified energy property which is installed on or in connection with a dwelling unit located in the United States and owned and used by the taxpayer as the taxpayer’s principal residence, and originally placed in service by the taxpayer. Such term includes expenditures for labor costs properly allocable to the onsite preparation, assembly, or original installation of the property.

“Qualified energy property” is defined as energy-efficient building property; a qualified natural gas, propane, or oil furnace or hot water boiler; or an advanced main air circulating fan.

Virginia Energy Star and WaterSense Sales Tax Holiday

Under Virginia law, the Energy Star and WaterSense Sales Tax Holiday is a recurring event, which begins on the Friday before the second Monday in October of every year and ends at midnight on the Monday immediately following. During this period, consumers may purchase certain Energy Star qualified products exempt of the Retail Sales and Use Tax. The exempt items include: any dishwasher, clothes washer, air conditioner, ceiling fan, compact fluorescent light bulb, dehumidifier, or refrigerator, the energy efficiency of which has been designated by the United States Environmental Protection Agency and the United States Department of Energy as meeting or exceeding each such agency’s requirements under the Energy Star program. The exemption is also available for WaterSense qualified products containing a WaterSense label. In order to be eligible for the Energy Star or WaterSense sales tax holiday exemptions, products must cost \$2,500 or less per item and be purchased for noncommercial home or personal use. The annual Energy Star and WaterSense Sales Tax Holiday is currently set to expire on July 1, 2017.

Virginia’s Clean Energy Manufacturing Incentive Grant Program

In April 2011, Virginia’s Clean Energy Manufacturing Incentive Grant Program was established to create a program that provides financial incentives to companies that manufacture or assemble equipment, systems, or products used to produce renewable or nuclear energy, or products used for energy conservation, storage, or grid efficiency purposes. A clean energy manufacturer can receive a grant for up to six years if, beginning on or after July 1, 2011, it meets all of the following criteria:

- Begins or expands its operations in Virginia;
- Makes a capital investment of more than \$50 million in Virginia;

- Creates 200 or more new full-time jobs; and
- Enters a memorandum of understanding setting forth the requirements for capital investment and the creation of new full time jobs.

The Governor, however, may reduce the capital investment and full-time job minimums if the manufacturer is located in an area with an unemployment rate of 1.25 times the statewide average unemployment rate of the previous year. For wind manufacturers, the capital investment minimum is \$10 million and the new full-time job minimum is 30.

Proposed Legislation

This bill would allow eligible taxpayers to claim a transferable credit against the individual income tax, the corporate income tax, and the insurance premiums license tax for placing renewable energy property into service in the Commonwealth during the taxable year. The tax credit would equal 40 percent of the costs paid or incurred by the taxpayer to place the property into service, not to exceed \$2.5 million for any individual piece of renewable property. Any costs related to existing infrastructure would not be eligible for the credit.

If the renewable energy property that is eligible for the credit is not in excess of \$250,000, the tax credit would be allowed for the taxable year in which the property is placed into service. For all other renewable energy property, the tax credit would be allowed in three equal taxable year installments, beginning with the taxable year in which the property is placed into service.

If any portion of the cost of the renewable energy property was funded directly or indirectly by Commonwealth of Virginia grants, Commonwealth of Virginia tax exempt bonds, utility ratepayer funds, or any other public funds, the amount of the tax credit otherwise allowed for the taxable year with respect to the renewable energy property would be a reduced credit amount computed by the following formula:

$$\text{Amount of Credit Otherwise Allowed} - (\text{Amount of Credit Otherwise Allowed} \times \text{Percentage of the Property Funded Publicly})$$

The Percentage of Property Funded Publicly would be a fraction, (i) the numerator of which is the sum, for the taxable year and all prior taxable years, of (a) grants provided by the Commonwealth for use in connection with the renewable energy property; (b) proceeds of obligations issued by the Commonwealth used to provide financing for the property, the interest of which is exempt from income taxation; (c) utility ratepayer funds for which the utility is guaranteed a rate of return by the State Corporation Commission; and (d) other public funds of the Commonwealth directly or indirectly provided in connection with the property and (ii) the denominator of which is the aggregate amount of additions to the capital account for the renewable energy property for the taxable year and all prior taxable years. The amounts included in the numerator and the denominator for any taxable year would be determined as of the close of the taxable year.

If, in one of the three taxable years in which the installment of a credit accrues, the renewable energy property is disposed of, taken out of service, or moved out of the Commonwealth, the credit would expire and the taxpayer would be subject to recapture

for any credit so claimed. However, the taxpayer would be permitted to claim any credit carried over from prior taxable years.

The amount of credit claimed would be limited to the amount of tax imposed upon the taxpayer for the taxable year. Any unused tax credit would be carried over for the next five succeeding taxable years or until the total amount of tax credit has been taken, whichever is sooner.

For purposes of this bill, “renewable energy” would be defined as energy derived from sunlight; wind; falling water; biomass, sustainable or otherwise; waster; landfill gas; municipal solid waste; wave motion; tides; or geothermal power. “Renewable energy” would not include energy derived from coal, oil, natural gas, or nuclear power.

The term “renewable energy property” would mean property that produces renewable energy and related devices necessary for collecting, controlling, storing, exchanging, conditioning, or converting such energy.

The term “individual piece of renewable energy property” would mean renewable energy property up to the point of existing infrastructure.

Any credit attributable to a partnership, electing small business corporation (S corporation), or limited liability company would be allocated to the partners, shareholders, or members, respectively, in proportion to their ownership or interest in such business entity.

Any taxpayer allowed a tax credit under this bill would be permitted to transfer or assign any unused but otherwise allowable portion of the credit to another taxpayer. The transferor or assignor taxpayer would be required to file a notification of such transfer or assignment with the Department of Taxation. Any proceeds realized by the transferor or assignor taxpayer would be exempt from taxation. The transferee or assignee taxpayer would be permitted to claim the tax credit for the taxable year in which the transfer or assignment occurs. Any unused tax credit would be carried over to succeeding taxable years, but in no event could the tax credit be claimed more than 11 years after it was originally allowed or in any taxable year of the transferee or assignee taxpayer that ended prior to the date of transfer.

The tax credit under this bill would be administered by the Department of Mines, Minerals, and Energy (“DMME”). The total amount of credits that DMME could approve in any given fiscal year would be limited to \$10 million. DMME would be required to develop procedures for allocating and awarding the tax credit under this bill. In order to claim a tax credit, taxpayers would be required to submit an application to DMME, including the construction permits needed to build the renewable energy property. Upon receipt of a complete application, DMME would be required to review and approve such application within 14 days. The taxpayer would then have 12 months from the date of allocation of the tax credits to place the renewable energy property into service. If the taxpayer fails to place the renewable energy property into service within 12 months, then the taxpayer’s allocation of tax credit would expire and the allocated tax credit amount would be added to the current fiscal year allocation of tax credits. Actions by DMME relating to the allocation

and awarding of credits under this bill would be exempt from the Administrative Process Act.

Taxpayers claiming this credit would submit with their applicable tax returns all documentation as required by the Department of Taxation.

The Department of Taxation in consultation with DMME would be required to develop, and update as necessary, guidelines implementing the provisions of this bill within ninety days of the bill's effective date. Such guidelines would be exempt from the Administrative Process Act.

This bill would be effective for taxable years beginning on or after January 1, 2014.

Similar Legislation

House Bill 910 would also create a renewable energy property tax credit; however, the total amount of credits that could be issued in any given fiscal year would be limited to \$100 million.

cc : Secretary of Finance

Date: 1/27/2014 mjm
SB653F161