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CANADIAN TAX *Highlights*

US Renewable Energy Incentives

The US federal government's policy for promoting the development and operation of renewable and alternative energy projects has materialized in new US tax laws. The Energy Improvement and Extension Act of 2008 (the 2008 Energy Act) extended and amended many tax incentives originally introduced under the Energy Policy Act of 2005 (the 2005 Energy Act). The American Recovery and Reinvestment Act of 2009 (the Stimulus Act) further expanded and extended the array of available tax incentives: (1) production tax credits; (2) investment tax credits; (3) for the first time, direct cash grants to the owners of certain renewable energy assets; and (4) accelerated tax depreciation of renewable energy assets. Permitting eligible taxpayers to apply for a cash grant in lieu of taking a tax credit reflects the effects of the economic downturn on businesses' ability to use certain tax credits. The legislation also permits a taxpayer to elect alternative credits, thereby providing flexibility for obtaining tax incentives.

Production tax credits and investment tax credits are two of the primary incentives for the production, development, and investment in renewable energy projects. A production tax credit (PTC) is an income tax credit for the production of electricity generated from qualified energy resources and sold to unrelated persons (a PTC) is provided in Code section 45 (originally enacted as part of the 2005 Energy Act and extended and modified in the 2008 Energy Act and the Stimulus Act). Qualified energy resources include wind, closed-loop biomass, open-loop biomass, geothermal energy, solar energy, small irrigation power, municipal solid waste, qualified hydropower production, and marine and hydrokinetic renewable energy. For 2009, the credit is 2.1 cents per kilowatt hour or 1.1 cents per kilowatt hour, depending on the source of production. The credit is adjusted for inflation; it is reduced for grants, tax-exempt bonds, and similar items; and it is allowed during the 10-year period from the date on which the facility was originally placed in service.

The Stimulus Act also extended and liberalized existing energy incentives. Specifically, renewable generation facilities eligible for the PTC may instead elect an upfront section 48 qualifying advanced energy project credit (an ITC) (a component of the section 38 investment credit). That ITC for any taxable year equals 30 percent of that year's qualified investment with respect to any qualifying advanced energy project of the taxpayer. Only that part of the basis of eligible property used in a qualified advanced energy project that was constructed, reconstructed, or erected (or acquired and placed in service) after 2008 and before 2017 is eligible for a section 48 ITC. A project must apply for and receive Treasury certification as a qualifying advanced energy project. Congress has authorized the Treasury to allocate up to an aggregate of $2.3 billion in ITCs for all taxpayers.

A taxpayer can now elect to treat a qualified facility as a qualified investment credit facility and take the ITC in lieu of the PTC. IRS Notice 2009-52 (2009-52 IRB 1094) prescribes the election procedure. The election, which is irrevocable, is available for facilities placed in service after 2008. The election provides a significant benefit for investors in wind facilities because under current business practice wind facilities, like solar facilities, may be leased or subject to a sale and leaseback, and under the ITC rules the developer of the facility can still benefit from the ITC.

The cash grant program in lieu of the ITC monetizes it for eligible taxpayers. The Stimulus Act allows taxpayers who are eligible for an ITC (including ITCs elected in lieu of PTCs) to receive instead an equivalent financial grant from the Treasury if the property is (1) placed in service in 2009 or 2010 or (2) placed in service before the credit termination date (January 1, 2013 for wind projects) and the property's construction began in 2009 or 2010. The Treasury must pay the grant within 60 days of the later of the date of application therefor and the facility's placed-in-service date. A grant is subject to the ITC recapture rules. A grant does not constitute taxable income, and the property's basis must be reduced by 50 percent of the grant. On July 9, 2009, the Treasury issued procedures for applying for payments and clarification of the eligibility requirements under the grant program.

The 2008 Energy Act provided additional energy-related benefits, such as a special deduction for energy-efficient commercial buildings and a 50 percent first-year bonus depreciation allowance for qualified reuse and recycling property. The Stimulus Act extends bonus depreciation for capital expenditures incurred in 2009; removes the dollar caps from the small-wind ITC; repeals subsidized energy financing limitations on the ITC; provides a 30 percent ITC for investment in property used in a qualified advanced energy manufacturing project; provides funding for workforce training for renewable energy and energy-efficiency careers as specified in the Green Jobs Act of 2007; and creates a loan guarantee program at the Department of Energy for commercial and innovative technologies, generation projects, and transmission and manufacturing facilities.

Many states also offer tax incentives for renewable energy projects and other green projects. The differences in incentives from state to state, as well as differences in non-tax considerations such as geography and business climate, make it important to analyze the full range of opportunities before locating a renewable energy project in the United States.

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