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KPMG report: Outlook for what's ahead for energy tax incentives (updated)

Coming off year-end extensions, the tax incentives for various renewable and clean energy sources and technologies could see an additional boost from Congress in the coming months.

This report briefly describes the potential for additional extensions and enhancements as proposals from the Biden Administration and Congress take shape.

Biden Administration plan

President Biden has described a two-step plan for "rescue and recovery" in response to the coronavirus (COVID-19) pandemic health and economic crises. With enactment of the "American Rescue Plan Act of 2021" on March 11, 2021, the focus can now shift to recovery.

President Biden on March 31, 2021, announced the "recovery" portion of his two-step plan that focuses on infrastructure, energy, innovation, and other areas. The available information about the plan does not include detailed descriptions, but does include the following energy related tax provisions:

- 10-year extension and phase down of an expanded direct-pay investment tax credit and production tax credit for clean energy generation and storage (paired with strong labor and collective bargaining standards for jobs created by the credits)
- Investment tax credit to mobilize private capital for the buildout of at least 20 gigawatts of high-voltage capacity power lines
- Reform and expansion of section 45Q credit for carbon capture projects
- Tax incentives "to buy American-made" electric vehicles
- Extend and expand home and commercial energy-efficiency tax credits
- Extend section 48C advanced manufacturing tax credit
- Repeal fossil fuel subsidies and reinstate superfund payments

Another notable feature of the Biden plan that could be an interesting companion to the enhanced tax incentives is the plan to establish the "Energy Efficiency and Clean Electricity Standard" (EECES). There are few details about how the EECES would operate, but it could act as a nation-wide standard requiring utilities to source electricity from specified cleaner resources, similar to renewable portfolio standards currently enacted in several states.

Additional details of the Biden plan are still taking shape but for an indication of how many of these provisions may work it is useful to look to recently introduced legislative proposals. Comprehensive extensions, enhancements, and reforms to the energy tax incentives have recently been proposed in the both the House of Representatives and the Senate.

The GREEN Act

In February 2021, Representative Mike Thompson, (D-CA), a member of the U.S. House of Representatives Committee on Ways and Means reintroduced the "Growing Renewable Energy and Efficiency Now" (GREEN) Act. The Biden plan's proposals related to energy seem to track the GREEN Act in many ways, which may make the GREEN Act a good early indicator of how the Biden plan will translate into legislative language.

- ***ITC and PTC***

  The GREEN Act would reinstate and extend the solar investment tax credit (ITC) at 30% for projects that begin construction before 2026, then phase down to 26% for projects that begin construction in 2026, 22% for projects that begin construction in 2027 and 10% thereafter.

  For wind, the GREEN Act would extend the current 60% production tax credit (PTC) for wind facilities that begin construction before 2027.

  The GREEN Act would extend the ITC and PTC for other eligible technologies and expand the ITC to include energy storage technology and linear generators.

- ***Direct pay***

  A significant feature of the GREEN Act is its inclusion of a "direct pay" provision allowing taxpayers to elect to treat 85% of the ITC and PTC as a payment of tax, entitling them to a refund to the extent the payment exceeds available tax liability. The direct pay provision would apply to projects placed in service after the date of enactment.

- ***Electric vehicles***

  The GREEN Act also includes proposals related to electric vehicles, which is another priority area for the Biden Administration. The proposal would extend and expand the existing electric vehicle credit, specifically by increasing the phase-out threshold and permitting used and large vehicles to be eligible for the credit. The GREEN Act would also allow manufacturers that have already passed the existing 200,000 vehicle threshold to continue to benefit from the credit.

- ***Other notable provisions***

  - Extension of the section 45Q credit for carbon oxide sequestration facilities that begin construction before the end of 2026 and provide an 85% direct-payment option
  - Extension and modification of residential energy and energy efficiency incentives
  - Additional allocation of section 48C advanced manufacturing credit, with prevailing wage requirement
  - Extension of excise tax credit for alternative fuels
  - Extension of availability of publicly traded partnerships for renewable energy projects

Senate Finance Chairman Wyden's proposals

Senate Finance Committee Chairman Ron Wyden (R-OR) on April 21, 2021 introduced a bill—the "Clean Energy for America Act''—that would aim to create a simpler set of long-term, performance-based energy tax incentives with the goals of being technology-neutral and to promote clean energy in the United States.

- ***ITC and PTC***

  The bill would replace the current renewable energy tax incentives with a new clean electricity PTC and ITC. The bill would allow taxpayers to choose between a 30% ITC or a PTC equal to 2.5 cents per kilowatt hour. The credits would apply to facilities with zero or net negative carbon emissions placed in service after December 31, 2022. The Wyden bill would also extend current tax credit provisions through December 31, 2022.

  The credits are set to phase out when certain emission targets are achieved, specifically when the Environmental Protection Agency and the Department of Energy certify that the electric power sector emits 75 percent less carbon than 2021 levels.

  Qualifying transmission grid improvements also would be eligible for the 30% ITC including standalone energy storage property. Storage technologies eligible for the ITC would not be required to be co-located with power plants and include any technologies that can receive, store and provide electricity or energy for conversion to electricity. Transmission property would include transmission lines of 275 kilovolts (kv) or higher, plus any necessary ancillary equipment. Regulated utilities would have the option to opt-out of tax normalization requirements for purposes of the grid improvement credit. The bill does not, however, include a similar opt-out of the tax normalization provisions for ITC for other types of qualifying facilities.

  Under the bill, investments qualifying for the clean emission investment credit, grid credit or energy storage property credit that are located in qualifying low-income areas would qualify for higher credit rates.

- ***Carbon capture***

  The section 45Q tax credit would be extended until the power and industrial sectors meet certain emissions goals; however, the bill would make some significant modifications to the credit, in particular, enhanced oil and natural gas recovery projects would no longer qualify for the credit.

  In addition, the credit amounts for direct air capture facilities would be significantly enhanced, and the bill would also modify the minimum capture thresholds. Under the proposed modified thresholds, in order to qualify for the section 45Q tax credit, electric generating facilities would be required to capture at least 75% of the CO2 that otherwise would be released into the atmosphere and industrial facilities would be required to capture at least 50% of the CO2 which would otherwise be released into the atmosphere. These changes would be effective for projects on which construction begins after December 31, 2021.

- ***Direct pay***

  The Wyden bill would provide taxpayers with the option of treating the ITC, PTC, and section 45Q credit as payments of tax; those wishing to avail themselves of this election would have to inform the Treasury Department **before** the facility to which the election relates begins construction. Unlike the GREEN Act, the Wyden bill would not impose a 15% haircut on the amount of the direct pay amount. Also, note that in the Wyden bill, the direct pay election and resulting refund would be allowed at the partnership level. Finally, the new ITC and PTC created by the bill, including the direct pay feature, would be effective for projects that are placed in service after December 31,

2022. For section 45Q, the direct pay provision would apply to projects that begin construction after December 31, 2021.

- ***Electric vehicles***

  The Wyden bill would modify and enhance the incentives available for electric vehicles. Specifically, the bill would repeal the per-manufacturer vehicle cap and make the credit refundable for individuals. Commercial operators would be able to claim non-refundable credit worth 30% of the purchase of an electric vehicle. The credits would phase out when the electric vehicles represent more than 50% of annual vehicle sales.

- ***Other notable provisions***

  - Taxpayers receiving credits to pay wages at not less than local prevailing rates and use registered apprenticeship programs
  - PTC for production of clean fuels
  - Incentives for energy efficient homes and commercial buildings and for clean transportation technologies
  - Tax credit bonds for facilities producing clean electricity or clean transportation fuels
  - Repeal of certain incentives for fossil fuels, including immediate expensing for intangible drilling costs, percentage depletion, deductions for tertiary injectants and credits for enhanced oil recovery, coal gasification and advanced coal projects; also repeal of the special treatment of fossil fuels under the publicly traded partnership rules

Table comparing various provisions

	Biden Plan	**GREEN Act**	**Wyden Plan**
ITC	10 yr extension and phase down; no info on credit amount; direct pay but no additional info	Generally provides 30% ITC if construction begins before 2026, then phases down to 10% for construction beginning after 2027; 85% direct pay	Any technology can qualify for ITC the credits as long as emissions at or below zero; 30% credit rate; 100% direct pay; credits will phase out based on emissions targets
PTC	10 yr extension and phase down; no info on credit amount; direct pay but no additional info	Generally extends PTC for projects beginning construction before 2026; credit rate at 60% of statutory rate; 85% direct pay	Any technology can qualify for PTC the credits as long as emissions at or below zero; 30% credit rate; 100% direct pay; credits will phase out based on emissions targets
Storage	Includes "storage" as part of credit proposal but no additional detail	ITC for storage; 85% direct pay	ITC for storage; Regulated utilities can elect out of tax normalization requirements; 100% direct pay
Transmission	ITC for buildout of at least 20 gigawatts of high-voltage capacity	Does not include transmission incentive	ITC for transmission investment; Regulated utilities can elect out tax normalization requirements; 100% direct

	power lines		pay
Carbon capture	"Reform and expand" the 45Q tax credit; add direct pay	Extend 45Q for projects on which construction begins before 2027; 85% direct pay	Section 45Q tax credit would be extended until the power and industrial sectors meet emissions goals; EOR no longer eligible; higher credit for direct air capture; modified minimum capture thresholds; 100% direct pay
Electric vehicles	Provide "tax incentives" to buy American made EVs	Modifies current law credits by increasing phase out limits; creates new credits for used and large electric vehicles	Makes credit refundable for individuals; commercial operators can claim 30% non-refundable credit; credits phase out when EVs represent more than 50% of annual vehicle sales
Manufacturing	Extend 48C	Extend 48C	No incentive for manufacturing
Fossil Fuel Subsidies	"Eliminate tax preferences for fossil fuels"	No provisions related to fossil fuels	Repeal fossil fuel preferences

KPMG observation

The common thread between the various proposals is the continued incentivization of clean energy development through the tax code. The tax credit regime has proven successful at encouraging new investment and the rules and the industry have evolved together. While the Biden Administration plan and the GREEN Act would mostly extend and enhance the existing tax credits, the Wyden bill—although still tax incentive-based—presents a departure of sorts.

Another common policy is the move toward making the tax credits refundable through a direct pay mechanism. It remains to be seen if and how refundability makes its way into law. Various justifications for direct pay include the limited tax liability of investors and the base erosion anti-abuse (BEAT) limitations on tax credits, but query whether potential higher tax rates and/or BEAT repeal make direct pay seem less necessary?

Finally, it will be interesting to monitor the development of some of the non-tax aspects of these proposals. Specifically will the inclusion of an EECES and strong labor standards become part of the ultimate package and, if so, how could that shape development going forward?

In terms of next steps, the Treasury Department will soon release a "Green Book" that will describe in more detail many of the proposals in the Biden plan. With that additional detail, larger negotiations will determine how the energy and tax portions of the ultimate legislative package take shape. The process is likely to be complicated and, of course, priorities could change during this time. That said, particularly in light of President Biden's recent commitment to reduce emissions by approximately half by 2030, the emphasis on clean energy is unlikely to subside.

For more information, contact a KPMG tax professional:

Hannah Hawkins | +1 (202) 533 3007 | hhawkins@kpmg.com
Katherine Breaks | +1 (202) 533 4578 | kbreaks@kpmg.com
Julie Marion | +1 (312) 665 1990 | juliemarion@kpmg.com
Kim Sucha | +1 (402) 661 5220 | ksucha@kpmg.com

Or contact the leader of KPMG’s Power and Utility Tax practice:

Glenn Todd | +1 (412) 232 1642 | gtodd@kpmg.com