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Open-Loop Biomass Facilities Federal Tax Credits, Grants and Incentives

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- Section 45 of the Internal Revenue Code provides a production tax credit (PTC) for electricity produced from open-loop biomass
- The PTC for any taxable year is equal to \$10 per megawatt
- Credit available for 10 years from placed in service date
- Facility must be placed in service before January 1, 2014

- Taxpayers may elect to claim a 30% ITC in lieu of PTCs for certain Section 45 facilities, including open-loop biomass, closed loop biomass, and municipal solid waste
- Available for facilities placed in service after 2008 and before the applicable Section 45 deadline
- Taxpayer cannot have claimed Section 45 PTCs
- Taxpayer must irrevocably elect to claim ITCs rather than PTCs
- Property will be treated as “energy property” for purposes of Section 48
 - Recapture
 - Tax-exempt use property rules
 - Sale-leaseback rules
 - Qualified progress expenditures

- Enacted in Section 1603 of the American Recovery and Reinvestment Tax Act of 2009
- 30% cash grant is provided for open-loop biomass facilities in lieu of 30% ITC or PTCs
 - Facility must be placed in service in 2009 or 2010
 - Facility can be placed in service prior to 2014 if construction began in 2009 or 2010
 - Construction of facility can have begun before 2009
 - Only property placed in service after 2008 will qualify for cash grant
- Applicants who receive a cash grant cannot also claim 30% ITC or PTCs

- Any agricultural livestock waste nutrients
 - Agricultural livestock includes bovine, swine, poultry, and sheep
 - Waste nutrients means manure and litter, including wood shavings, straw, rice hulls, and other bedding material for the disposition of manure
- Any solid, nonhazardous, cellulosic waste material or any lignin material which is derived from—
 - Certain forest-related resources: Mill and harvesting residues, precommercial thinnings, slash, and brush
 - Solid wood waste materials: Includes waste pallets, crates, dunnage, manufacturing and construction wood wastes (other than pressure-treated, chemically-treated, or painted wood wastes), and landscape or right-of-way tree trimmings; excludes municipal solid waste, gas derived from the biodegradation of solid waste, paper which is commonly recycled
 - Agriculture sources: Orchard tree crops, vineyard, grain, legumes, sugar, and other crop by-products or residues
 - Includes wood bark and lignin material recovered from spent pulping liquors

- All other facilities using open-loop biomass to produce electricity must be originally placed in service before January 1, 2011
- Special exception to tax ownership rule for lessees and operators of open-loop biomass facilities
- Special rule for expansions of facilities
 - “Facility” includes a new unit placed in service after October 3, 2008 in connection with an existing open-loop biomass facility, but only to the extent of the increased amount of electricity produced at the facility by reason of such new unit

- IRS issued interim guidance (Notice 2008-60, superceding Notice 2006-88) regarding electricity produced from open-loop biomass
- IRS indicates it will issue regulations for open-loop biomass
 - Chances of regulations being issued?
 - Notice is published guidance on binding on IRS but is not entitled to the level of deference given to a regulation
- Notice 2008-60 states that the IRS will not issue PLRs regarding Section 45 as it relates to open-loop biomass
- Notice 2008-60 also states that the IRS will not rule on any issues under Subchapter K for partnerships claiming the credit under Section 45
- No guidance on tax credits claimed by lessees or operators of open-loop biomass facilities

- Power plant consisting of all components necessary for the production of electricity from open-loop biomass (and, if applicable, other energy sources)
- Includes:
 - All burners and boilers (whether or not burning open-loop biomass)
 - Any handling and delivery equipment that supplies fuel directly to and is integrated with such burners and boilers
 - Steam headers, turbines, generators, and all other depreciable property necessary to the production of electricity

- Excludes:
 - Property used for the collection, processing, or storage of open-loop biomass before its use in the production of electricity
 - Transformers or other property used in the transmission of electricity after its production
 - Ancillary site improvements (*e.g.*, roadways and fencing) that are not necessary to the production of electricity
- Each power plant that is operated as a separate integrated unit is treated as a separate facility

- Notice 2008-60 adopts the 80/20 test of Revenue Ruling 94-31 in determining whether an existing facility has acquired a new placed-in-service date
- Under Revenue Ruling 94-31, property is treated as having acquired a new placed-in-service date, even if it contains some existing components of a facility, provided the fair market value of the existing components is not more than 20% of the facility's total value (the cost of the new property plus the value of the used property)
- Notice 2008-60 refers to the test in the negative: the facility will not be treated as originally placed in service after October 22, 2004 or August 8, 2005, as the case may be, if more than 20 percent of the facility's total value (the cost of the new property plus the value of the used property) is attributable to property placed in service on or before such date

- The term “open-loop biomass” does not include “closed-loop biomass or biomass burned in conjunction with fossil fuel (cofiring) beyond such fossil fuel required for startup and flame stabilization.”
- Notice 2008-60 states that biomass will qualify as open-loop biomass only if the amount of fossil fuel used is “the minimum necessary for startup and flame stabilization.”
 - “minimum necessary” is not defined or illustrated
 - only the electricity produced from the open-loop biomass can qualify for the credit and electricity produced from the fossil fuel used for startup and flame stabilization does not qualify for the credit
 - allocation based on thermal content from open-loop biomass
- If biomass is cofired with fossil fuels beyond the minimum amount necessary, “the biomass is not open-loop biomass and the electricity produced from the biomass does not qualify for the § 45 credit”

- Cofiring with other biomass or non-fossil fuel materials: Permissible? Determination of credit amount?
- Notice 2008-60 provides that electricity produced from open-loop biomass that is cofired with fuels other than fossil fuels may qualify for the Section 45 credit
- Electricity produced from the other fuel may also qualify for credits if it is also a qualified energy resource and the facility is placed in service during the period specified for that qualified energy resource
 - Cofiring with fuels that do not meet these requirements should not impact open-loop biomass-generated electricity's qualification for credits
 - Allocation based on thermal content of fuels
 - Example: Facility co-firing open-loop biomass with tire-derived fuels

- Defined by reference to the term “solid waste” under section 2(27) of the Solid Waste Disposal Act (42 U.S.C. 6903):
 - any garbage, refuse, sludge from a waste treatment plant, water supply treatment plant, or air pollution control facility and other discarded material, including solid, liquid, semisolid, or contained gaseous material resulting from industrial, commercial, mining, and agricultural operations, and from community activities, but does not include solid or dissolved material in domestic sewage, or solid or dissolved materials in irrigation return flows or industrial discharges which are point sources subject to permits under 33 U.S.C. 1342, or source, special nuclear, or byproduct material as defined by the Atomic Energy Act

- Trash Facilities: In the case of a facility which uses municipal solid waste to produce electricity, the term “qualified facility” means any facility owned by the taxpayer which is originally placed in service after October 22, 2004 and before January 1, 2011
- The definition of “trash facility” was clarified to provide that the trash does not have to be burned/combusted directly to produce electricity in order to qualify, but can be gasified and the gas used to produce electricity. This provision is effective for electricity produced and sold after 10/3/08

- Private Letter Ruling regarding a facility that used both open-loop biomass and MSW to produce electricity
- PLR allowed gasification of MSW, but the Stabilization Act clarified this issue.
- IRS refused to rule on any open-loop biomass issues
- IRS refused to issue a partnership related ruling (Section 708(b)(1)(B)).
- IRS ruled that taxpayer could claim Section 45 tax credits for electricity generated at the facility, and sold to unrelated parties, net of any electricity supplied from the grid for use in the plant.
 - However, the “net sales rule” was deleted in Notice 2008-60

- “Closed-loop biomass” means “any organic material from a plant which is planted exclusively for purposes of being used at a qualified facility to produce electricity.”
 - Switchgrass mentioned in legislative history
 - Does not include standing timber
- In the case of a facility using closed-loop biomass to produce electricity, the term “qualified facility” means any facility owned by the taxpayer which is originally placed in service after December 31, 1992, and before January 1, 2008

- Section 45(d)(2)(A)(ii) provides special rules for facilities modified to co-fire closed-loop biomass with coal, with other biomass, or with both:
 - Applies to coal-burning facilities originally placed in service and modified before January 1, 2008
 - Modification must be approved under the Biomass Power for Rural Development Programs or be part of a pilot project of the Commodity Credit Corporation as described in 65 Fed. Reg. 63052
 - Section 45 credit equals normal Section 45 tax credit amount multiplied by the ratio of the thermal content of the closed-loop biomass used in such facility to the thermal content of all fuels used in such facility
 - Special exception to tax ownership rule for lessees and operators of the co-firing facility