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VanNess Feldman

Chairman Baucus Releases Energy Tax Reform Draft

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Yesterday, Senate Finance Committee Chairman Max Baucus (D-MT) released the fourth in a series of discussion drafts to overhaul America's tax code. This draft outlines energy tax reforms that would eliminate 42 existing energy tax incentives and replace them with two technology neutral tax incentives: one for clean generation of electricity and one for the production of clean transportation fuels. Chairman Baucus has requested that comments on the draft proposals and on several specific issues raised in the draft summary be submitted to the Senate Finance Committee staff by January 31, 2014.

Late yesterday also brought the unexpected news that Senator Baucus would be nominated to be Ambassador to China as early as today. If this proves to be true, then Senator Baucus will be leaving the Senate early in 2014, thus putting the likelihood of tax reform in 2014 even more in doubt; Senator Wyden (D-OR) likely would become Chairman of the Senate Finance Committee; and Senator Landrieu (D-LA) likely would become Chairman of the Senate Energy and Natural Resources Committee.

Regardless of the developments with regard to Chairman Baucus, these draft proposals are now on the table and must be analyzed for their potential effect and should be either supported or opposed in written comments to the Finance Committee staff by January 31, 2014. Senator Wyden has said these proposals are a promising start toward his goal of technology neutral incentives that encourage reductions in greenhouse gas emissions.

THE BAUCUS ENERGY TAX PROPOSALS

"It is time to bring our energy tax policy into the 21st century," Senator Baucus said. "Our current set of energy tax incentives is overly complex and picks winners and losers with no clear policy rationale. We need a system of energy incentives that is more predictable, rational, and technology-neutral to increase our energy security and ensure a clean and healthy environment for future generations."

Tax Incentive for Electricity Generation

The draft legislation proposes to extend the existing production tax credit (PTC) and investment tax credit (ITC) for electricity generation to facilities placed in service prior to January 1, 2017. For facilities placed in service after December 31, 2016, the proposal replaces the existing incentives with a technology neutral incentive that would apply to a facility that produces electricity that is at least 25% cleaner than the average for all electricity production facilities. The maximum credit for a zero emission facility would be 2.3 cents (adjusted for inflation) per kilowatt-hour for the PTC or 20% for the ITC. The PTC can be claimed on electricity generated by a single facility for a maximum of 10 years. The new technology neutral credit would provide about the same level of PTC as the existing credit for solar and wind industry, while the ITC would be reduced from the current 30% to 20%. The new credits would phase out over four years once the greenhouse gas intensity of all U.S. electricity generation declines to a point that it is 25% cleaner than in 2013.

Tax Incentive for Transportation Fuels

On the transportation side, the draft proposes to extend the incentives of current law for biodiesel and renewable diesel and the second generation biofuel credit through December 31, 2016. After December 31, 2016, the draft would replace these existing incentives with a new technology neutral incentive. Under the draft, a business can choose between a production tax credit (PTC) or an investment tax credit. The maximum credit for a fuel with the same energy content as gasoline and with zero lifecycle emissions would be $1.00 per gallon (adjusted for inflation) for the PTC and 20% of the cost of the investment for the ITC. The amount of the allowable PTC or ITC would be reduced depending on the fuels energy content and emissions when compared to that for conventional gasoline. The new PTC is effective for fuel sold or used after December 31, 2016 and the ITC is effective for facilities placed in service after December 31, 2016. The new transportation fuel incentive does not have a fixed expiration date, however it would be phased out over four years once greenhouse gas intensity of all transportation fuels has declined to a level that is 25% cleaner than conventional gasoline.

Specific Issues for Which Comments are Sought

The discussion draft lists several areas in which Chairman Baucus and the Senate Finance Committee staff would like comments on issues raised or left out of the draft. They would like comments on:

- the merits of providing incentives for clean energy technology versus a tax or fee on heavy polluting technologies or air pollution;
- other ways to determine when the incentives should be phased-out;
- allowing existing facilities to qualify for the incentive if they convert to clean generating facilities (how should the policy be designed);
- whether proposed recapture provisions are appropriate;
- on how to most effectively design a pre-certification process for new technology; and
- whether 50% capture is the appropriate threshold for allowing the ITC on retrofitting existing facilities for carbon capture technology, whether the credit should be performance based, and will it effectively promote the adoption of carbon sequestration technologies.

Comments on the proposals in the draft and on these specific issues should be submitted to the Senate Finance Committee by January 31, 2014.

DOCUMENTS AVAILABLE FROM THE SENATE FINANCE COMMITTEE

The following documents describing the proposals in the discussion draft are available on the Senate Finance Committee website:

- Energy Tax Reform Discussion Draft Summary
- Energy Tax Reform Discussion Draft One Pager
- Energy Tax Reform Legislative Language
- JCT Technical Explanation of Energy Tax Reform Discussion Draft

POSSIBLE FUTURE DEVELOPMENTS

This is the fourth in a series of discussion drafts that Chairman Baucus has issued (the first three were issued in November) and he had said he planned to issue additional drafts on other issue areas. Once the comments had been received on all the drafts, the Committee staff would then have begun to develop final legislative proposals to create a comprehensive tax reform package that would have been introduced sometime in 2014, but most likely around the end of the first quarter.

In light of the high likelihood that Chairman Baucus will be leaving the Senate early in 2014 to become Ambassador to China, it is not yet clear that his successor, who is presumed to be Senator Wyden (D-OR), will adopt Chairman Baucus' plan of action.

Regardless of a change in Senate chairmanships, 2014 will be a pivotal year in the Congressional efforts to enact comprehensive tax reform or, at a minimum, enacting an extension of the expiring tax provisions, including several energy-related tax provisions, while laying the groundwork for tax reform in the next Congress. Proposals that have been made public to date must be analyzed and a response developed; these proposals could reappear later when the tax reform debate is well underway.

FOR MORE INFORMATION

If you need assistance in developing comments on the energy tax reform draft, previous drafts that have been released by Chairman Baucus or additional information on comprehensive tax reform or expiring tax provisions, please contact Michael Platner (mlp@vnf.com) or your relationship partner at Van Ness Feldman, LLP.