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Taxation Section

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The Oregon Business Energy Tax Credit

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The Oregon Business Energy Tax Credit (“BETC”) is a nonrefundable credit against Oregon personal and corporate income taxes based on the “certified cost” of certain investments in energy conservation, recycling, renewable energy resources, or reduced use of polluting transportation fuels. Originally enacted in 1979, the BETC was significantly expanded in 2007,¹ and expanded again in 2008,² as part of an effort to encourage alternative energy development. The BETC is available only for investments in facilities that are completed by the end of 2015.³

This article will summarize (1) the structure of the BETC statutory provisions, (2) the types of investments that are eligible for the BETC, (3) the amount of BETC allowable with respect to particular investments, (4) the process for obtaining BETC certification of an investment, (5) the monetization of the BETC through the so-called “pass-through” program, and (6) areas of uncertainty in the BETC rules.

Structure of the BETC Statutory Provisions and Administrative Oversight

The BETC is allowed under ORS 315.354. Most of the statutory rules relating to the BETC, however, are contained in ORS Chapter 469. The link between ORS Chapters 315 and 469 is established by two provisions in ORS 315.354. First, ORS 315.354(1) provides that the allowable BETC is “based upon the certified cost of the facility during the period for which that facility is certified under ORS 469.185 to 469.225.” Second, ORS 315.354(3) provides: “In order for a tax credit to be allowable under this section *** (b) [t]he facility must have received final certification from the Director of the State Department of Energy under ORS 469.185 to 469.225; and (c) [t]he taxpayer must be an eligible applicant under ORS 469.205(1)(c).”

The Department of Revenue has issued limited guidance under ORS 315.354, deferring to the Department of Energy (the “DOE”). In particular, OAR 150-315.354(2) provides: “For facilities receiving preliminary or final certifications issued by the Office of Energy on or after January 1, 2001, the credit may be claimed by eligible applicants under ORS 469.205(1)(c) and the related administrative rules. See Chapter 330, Division 90 of the Oregon Administrative Rules (e.g., OAR 330-90-0105) for additional information.”

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Due to the certification requirements set forth in ORS 315.354, the DOE has a substantial “gatekeeper” role in the allowance of BETCs. Thus, projecting BETCs with respect to an alternative energy project is more speculative than projecting energy-related federal income tax credits, which may be claimed on a federal income tax return based on the taxpayer’s own determination that it is eligible for the claimed credits.⁴

Investments Eligible for BETCs

BETCs are available with respect to a wide array of “green” investments (referred to as “facilities” under the BETC rules), including certain investments, made in connection with a trade or business, that accomplish any of the following objectives:⁵

- Use of a renewable energy resource or solid waste instead of electricity, petroleum, or natural gas.
- Use of a renewable energy resource in the generation of electricity for sale or to replace an existing or proposed use of an existing source of electricity.
- Substantial reduction of the consumption of purchased energy.
- Acquisition, construction, or installation of equipment for recycling.
- Acquisition of an alternative fuel vehicle or conversion of an existing vehicle to an alternative fuel vehicle.
- Acquisition, construction, or installation of a facility necessary to operate alternative fuel vehicles.
- Acquisition of transit passes for use by specified individuals.
- Acquisition of a sustainable building practices facility.
- Acquisition of a car sharing facility and operate a car sharing program.
- Construction of a high-efficiency combined heat and power facility.
- Construction of a homebuilder-installed renewable energy system.
- Construction of a home meeting standards for reduced energy consumption established by the Department of Energy.

- Acquisition, construction, or installation of a renewable energy resource equipment manufacturing facility.

Amount of the BETC

The amount of the BETC allowed with respect to a facility in each taxable year is based on (1) percentages and timing rules set forth in ORS 315.354, (2) the final cost for the facility certified by the DOE under ORS 469.215 (which is limited by the maximum eligible cost for the facility under ORS 469.200), and (3) the period for which the DOE’s cost certification is effective, as determined under ORS 469.220.

The maximum BETC allowable with respect to a facility depends on the nature of the facility. In the case of a facility that “uses or produces renewable energy resources or is a renewable energy resource equipment manufacturing facility,” the allowable BETC is 10% of the facility’s certified cost per year for five years, for a total of 50%. ORS 315.354(1)(c). In the case of an eligible renewable energy system installed by a homebuilder in a single-family dwelling, the maximum allowable BETC is \$9,000 per dwelling (or \$12,000 if the dwelling is a “high-performance home”). ORS 315.354(2) and (4). In the case of any other facility, the allowable BETC is 10% of the facility’s certified cost in the first two years of the five-year period for which the certification is effective, and 5% in each of the remaining three years, for a total of 35%. ORS 315.354(1)(a).⁶

In all cases, a taxpayer’s BETC for a taxable year may not exceed the taxpayer’s Oregon income tax liability. Any amount that is not allowed for a taxable year by reason of this limitation may be carried forward for eight years. ORS 315.354(6).

Process for Obtaining BETC Certification for a Facility

The process of obtaining BETC certification from the DOE for a facility involves two steps. First, the owner of the facility must complete an application for preliminary certification and submit it to the DOE, together with a supplementary information form and a fee to cover the review of the application. The information that must be provided in the application includes owner information, site location, construction dates, a description of the project, economic data, and estimated project costs. ORS 469.205;

OAR 330-090-0130. The DOE generally requires the application to be submitted before work commences on a project. OAR 330-090-0130(3).

Under OAR 330-090-0130(3), within 60 days after the application for preliminary certification is filed, the DOE will “decide if it is complete,” and the DOE will act on the application “within 120 days after a completed application is filed.” According to the DOE’s application forms, review of the application usually take four to six weeks to complete. If a preliminary certification is issued, it will specify “the amount of the tax credit approved” and also will state “any conditions that must be met before development, final certification, or some other event can occur.” OAR 330-090-0130(3)(b)(A).

If, during the course of construction, it appears that project costs will exceed the amount stated in the preliminary certificate, the project owner may apply for an amended preliminary certificate by submitting written documentation of the increased costs. OAR 330-090-0130(7).

While a project owner may begin (and even complete) work on a project before receiving a preliminary certification, there is no guarantee that a project will be approved for the BETC.

Once the project owner has obtained preliminary certification and has completed the project, the owner must file a final certification application. This application includes an affirmation that the project complies with conditions of the preliminary certificate and a verification of actual project costs. The amount of BETC certified by the final certificate may be as much as 10 percent more than the amount approved in the preliminary certificate. OAR 330-090-0130(9)(b)(A).

Monetization of the BETC Through the “Pass-Through” Program

Under ORS 469.206, “[t]he owner of a facility may transfer a tax credit for the facility in exchange for a cash payment equal to the present value of the tax credit.” The DOE refers to the transfer of the BETC as a “pass-through” and refers to the transferee as a “pass-through partner.”

Based on permissive authority in ORS 469.206(2), the DOE has issued rules arbitrarily determining

the “present value” of the BETC for purposes of this rule (referred to by the DOE as the “pass-through rate”). Under OAR 330-090-0140(1), in the case of projects with certified costs exceeding \$20,000, a pass-through partner must pay the project owner an amount equal to 33.5% of eligible costs in exchange for a transfer of the 50% BETC, and 25.5% of eligible costs in exchange for a transfer of the 35% BETC. In the case of projects with certified costs of \$20,000 or less, the pass-through rate is 43.5% in the case of the 50% BETC and 30.5% in the case of the 35% BETC.

If a project owner chooses to transfer the BETC to a pass-through partner, the pass-through partner must be identified when the final certification application is filed, and the pass-through partner must file a pass-through option application form. OAR 330-090-0130(8).

If an owner desiring to use the pass-through option has completed its project but has not yet secured a pass-through partner, the DOE will place the application on hold until a partner is identified. When a pass-through partner is secured and the “Application for Final Certification for Pass-through Projects” is completed and signed, the DOE issues a letter to both the project owner and the pass-through partner verifying the final eligible costs, the pass-through amount, and the tax credit amount. The pass-through partner gives the project owner the lump-sum cash payment indicated on the letter and the project owner notifies the DOE that the pass-through payment has been received. The DOE then issues a tax credit certificate in the name of the pass-through partner.⁷

Areas of Uncertainty

The extent of the DOE’s discretion to impose conditions on project owners and others in connection with the certification of project costs for the BETC is unclear. ORS 469.205(2)(f) provides that an application for preliminary certification shall include “[a]ny other information the [DOE] considers necessary to determine whether the proposed facility is in accordance with the provisions of ORS 469.185 to 469.225, and any applicable rules or standards adopted by the [DOE].” ORS 469.210(2) provides: “If the [DOE] determines that the proposed acquisition, erection, construction or installation is technically feasible and should operate in accordance with

the representations made by the applicant, and is in accordance with the provisions of ORS 469.185 to 469.225 and any applicable rules or standards adopted by the [DOE], the [DOE] shall issue a preliminary certificate approving the acquisition, erection, construction or installation of the facility.” ORS 469.197, adopted in 2007 and recently amended by HB 3619, establishes economic-impact criteria that DOE may take into account in certifying renewable energy resource manufacturing facilities, but that provision does not apply to the certification of other types of facilities. Ultimately, it is not clear whether the DOE has the authority to impose conditions or standards other than conditions and standards that implement the provisions of ORS 469.185 to 469.225. It also is not clear whether the DOE may impose conditions on certification other than through the rule-making process. There is no case law regarding the scope of the DOE’s authority to impose conditions on the certification of facilities for the BETC.

Another area of uncertainty is the ability of S corporations and entities that are taxed as partnerships for federal income tax purposes to obtain final certification of facilities for the BETC or to be transferees of BETCs under the pass-through program.

The instructions for Form 65 (Oregon Partnership Return of Income) state: “Partners may qualify for the following tax credits on their individual income tax returns even though the costs were paid by the partnership. *** Business energy.”

Nonetheless, in a proposed OAR dated December 1, 2007, and most recently reissued in proposed form on January 14, 2008, the DOE included definitions that would prevent a partnership, or a limited liability company (“LLC”) taxed as a partnership, from applying for final BETC certification.

Proposed OAR 330-090-0110(4) provides, in part:

(b) A person who applies for a final certification of a Business Energy Tax Credit under this section:

(A) Must be a taxpayer
(see definition for “Taxpayer”).

Proposed OAR 330-090-0110(69) provides:

“Taxpayer” means an individual, estate, or trust subject to tax under ORS Chapter 316, or a corpo-

ration subject to tax under ORS Chapters 317 or 318. The term does not include partnerships or other entities not subject to tax.

Under these proposed definitions, an S corporation, a partnership, or an LLC taxed as a partnership would be permitted to file an application for preliminary certification but would not be permitted to file an application for final certification. The proposed OARs were criticized at the DOE’s public hearing on January 15, 2008, and the DOE subsequently announced that it would not release the final OAR on February 1, 2008, as originally planned. The rule-making may be monitored at the following page on the DOE website: <http://www.oregon.gov/ENERGY/CONS/Rulemaking2007-BETC.shtml>.

Concluding Comments

The BETC is a powerful stimulus for the development of renewable energy resources and the “alternative” energy industry in Oregon. BETCs, in combination with Federal tax credits and other available subsidies, can reduce the after-tax cost of many alternative energy investments to a fraction of actual construction and installation costs. At present, the utilization of BETCs by developers of many alternative energy projects is hampered by uncertainty regarding the DOE’s exercise of its regulatory authority. Hopefully, those uncertainties will be resolved in the coming months.

Endnotes

- 1 See HB 3201, which may be viewed at the following address: <http://www.leg.state.or.us/07reg/measpdf/hb3200.dir/hb3201.en.pdf>.
- 2 See HB 3619, which may be viewed at the following address: <http://landru.leg.state.or.us/08ss1/measpdf/hb3600.dir/hb3619.en.pdf>.
- 3 Section 26, chapter 843, Oregon Laws 2007.
- 4 See, e.g., Internal Revenue Code sections 45 (production tax credit for electricity produced from certain renewable resources) and 48 (investment tax credit for certain energy property).
- 5 See ORS 469.185 and ORS 469.205(2)(a).
- 6 Both the 50% credit and the 35% credit are allowed in their entirety in the first year of the five-year period for which the certification is effective if the certified cost of the facility in question does not exceed \$20,000. ORS 315.354(1)(b).
- 7 See the DOE’s web page titled “Business Energy Tax Credit Pass-Through” at <http://www.oregon.gov/ENERGY/CONS/BUS/tax/pass-through.shtml>.