



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

January 28, 2013

The Honorable David Vitter
United States Senate
Washington, DC 20510

Dear Senator Vitter:

I am responding to your letters to Secretary Geithner discussing the Administration's renewable energy and climate policies.

Your November 20, 2012, letter makes reference to the Office of Environment and Energy at Treasury. This office was established by Secretary Paulson during the Bush Administration in 2008. Its eight-person staff focuses predominantly on international policy issues, and does not take the lead within Treasury in developing and analyzing new tax policies or reforms to the tax system.

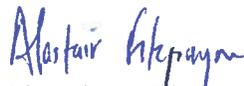
The Administration has not proposed a carbon tax. It is important to emphasize, however, that the Administration takes climate change seriously and has undertaken a number of steps to address the problem. For example, the Administration has made important investments in clean energy, and the United States has nearly doubled renewable energy generation since 2008. Higher fuel economy standards for passenger vehicles and new fuel economy standards for heavy-duty vehicles will save Americans money at the pump, reduce our imports of foreign oil, and reduce harmful greenhouse gas emissions. The most current testimony by the staff of the Treasury Office of Tax Policy on energy tax issues is enclosed.

Your January 14, 2013, letter asks about progress made “on a vow to generate \$100 billion annually by 2020” through a “\$100 billion international climate fund.” Despite inaccurate press reporting, there is no \$100 billion fund. Rather, developed countries have agreed to a goal of jointly mobilizing \$100 billion annually for developing countries by 2020. We anticipate that the vast majority of the funds to meet this goal will come from the private sector and a small portion will come from public funds. The United States has also been involved in setting up a multilateral Green Climate Fund (GCF), which is intended to strategically use limited public resources to catalyze and leverage private investment as one part of the larger mobilization effort. The United States is only one of many countries that may consider contributions to the GCF. We have not yet made any funding commitments and will continue to work closely with Congress in considering any future commitments.

Finally, with regard to your query concerning the Freedom of Information Act (FOIA) request submitted by the Competitive Enterprise Institute (CEI), the Treasury Department has granted a fee waiver to CEI and is working to respond to its request as expeditiously as possible. The Treasury Department is committed to fulfilling its obligations under FOIA, successfully reducing its FOIA backlog by 52 percent between 2009 and 2012. The Treasury Department has made significant progress in fulfilling the President's commitment to open and transparent government, providing access to as much information as possible while ensuring the protection of personal privacy, and confidential, privileged, and proprietary information. In fact, Treasury was one of six Cabinet-level departments recently to receive an "A" or better rating from the House Oversight and Government Reform Committee with respect to its tracking and management of FOIA requests.

Thank you again for your interest in this matter. Please feel free to contact us if you have further questions.

Sincerely,



Alastair M. Fitzpayne
Assistant Secretary for Legislative Affairs

Enclosure: April 2012: Deputy Tax Legislative Counsel John Parcell House Science Committee for their hearing on the "Impact of Tax Policies on the Commercial Application of Renewable Energy Technology."

**STATEMENT OF JOHN H. PARCELL
DEPUTY TAX LEGISLATIVE COUNSEL
DEPARTMENT OF THE TREASURY
BEFORE THE
HOUSE COMMITTEE ON SCIENCE, SPACE, AND TECHNOLOGY
SUBCOMMITTEE ON INVESTIGATIONS AND OVERSIGHT
AND
SUBCOMMITTEE ON ENERGY AND ENVIRONMENT**

April 19, 2012

Good morning Chairman Broun, Chairman Harris, Ranking Member Tonko, Ranking Member Miller, and members of the Subcommittees. Thank you for inviting me to testify before your Subcommittees today. I appreciate this opportunity to discuss the energy proposals in the President's FY 2013 Budget.

Overview of the Administration's Environmental and Energy Policy

First, I will briefly discuss the Administration's environmental and energy policy in order to provide context for a discussion of tax incentives for renewable energy.

The Administration believes in an all-of-the-above energy strategy – a strategy that relies on producing more oil and gas here in America, but also producing more wind power, more solar power, other renewable power, more fuel-efficient cars, and energy efficiency improvements. The American Recovery and Reinvestment Act of 2009 (Recovery Act) took an important step in that direction by providing more than \$80 billion for investment in clean energy technologies. As a result, the United States has nearly doubled renewable energy generation since 2008. Since 2009, the Department of Interior has approved 29 onshore renewable energy projects on public lands with a total capacity of 6,000 megawatts. Through loan programs, the Department of Energy has supported nearly 40 clean energy projects. Some of these are expected to generate enough clean electricity to power nearly 3 million homes. Others are expected to displace nearly 300 million gallons of gasoline annually. These loan programs support the world's largest wind farm, the first new U.S. nuclear plant in three decades, and several of the world's largest solar photovoltaic generation facilities. In addition, the Administration has proposed new fuel economy standards that by 2025 will require automobile fleets to average 54.5 miles per gallon. The new standards will save consumers \$1.7 trillion at the pump – roughly \$8,200 per vehicle. In addition, the new standards will reduce oil consumption by 2.2 million barrels per day by 2025 and reduce greenhouse gas emissions by 6 billion metric tons over the lifetime of vehicles covered by the new standards. The President has also called on Congress to invest in a new HomeStar program of rebates for consumers who make energy efficiency retrofits to their homes. Such a program will harness the power of the private sector to help drive consumers to make energy-saving and cost-saving investments in their homes.

Budget Tax Proposals Relating to Energy

With this as background, let me turn to the tax proposals in the President's FY 2013 Budget relating to energy. More details on the proposals (other than those that involve only an extension of an existing tax provision) can be found in the Appendix.

1. Provide additional tax credits for advanced energy manufacturing facilities

The Recovery Act provided \$2.3 billion in tax credits for investments in advanced energy manufacturing facilities. The credit, under section 48C of the Internal Revenue Code (Code), was designed to help our country take the lead in the manufacture of wind turbines, solar panels, electric vehicles, and other clean energy and energy conservation products. Eligible manufacturers receive a 30-percent credit for their investments in facilities to manufacture these products.

The Treasury Department and the Department of Energy cooperated to award the \$2.3 billion of credits authorized by the Recovery Act. Credits were awarded to 183 projects in 43 states to support tens of thousands of high quality clean energy jobs and the development of a domestic clean energy manufacturing base.

The \$2.3 billion cap on the credit has resulted in the funding of less than one-half of the technically acceptable applications that were received. The President's FY 2013 Budget proposes an additional \$5 billion in credits that would support at least \$15 billion in total capital investment. Because there is already an existing pipeline of worthy projects and substantial interest, the additional credit could be deployed quickly to create jobs and support economic activity.

2. Extend and modify renewable energy incentives

A production tax credit (Code section 45) is provided for the production of renewable energy from wind, solar, biomass, and various other sources. For most facilities, including wind facilities, the credit rate is 2.2 cents per kilowatt hour¹ and the credit is allowed for the electricity produced at a facility for the first ten years after it is placed in service. In addition, an investment tax credit (Code section 48), generally at a 30-percent rate, is available for energy property. Energy property includes any property that is part of a facility that could qualify for the production tax credit as well as certain other listed energy-related property. (A taxpayer must choose between the production tax credit and the investment tax credit and may not claim both credits for the same facility.) Finally, section 1603 of Division B of the Recovery Act requires the Treasury Department to make payments, generally at a 30-percent rate, to persons that place in service property that would otherwise qualify for the investment tax credit for energy property (the section 1603 program). (Again, a taxpayer must choose between the payment, the investment tax credit, and the production tax credit, and may not claim more than one of the incentives for the same facility.) To date, the section 1603 program has helped fund over 34,000 projects located in every state.

¹ The rate is subject to an annual inflation adjustment.

The production credit is available for wind facilities placed in service before the end of 2012 and for other renewable energy facilities placed in service before 2014. The investment tax credit is also available for these facilities. Certain other property may qualify for an investment tax credit even if placed in service after 2013. For example, the investment credit is available for solar facilities at a 30-percent rate through 2016 and at a 10-percent rate thereafter. Payments under the section 1603 program are subject to the same expiration dates as the investment tax credit, with two exceptions. First, no payments are allowed under the section 1603 program for property placed in service after 2016. Second, no payments are allowed for property placed in service after 2011 unless construction of the property began during 2009, 2010, or 2011.

Investments in property qualifying for these renewable energy incentives further the Administration's policy of supporting a clean energy economy, reducing reliance on oil, and cutting greenhouse gas emissions. The extension of incentives for these investments is necessary to the continued success of that policy.

The President's FY 2013 Budget would extend the production tax credit for wind facilities and the investment tax credit for wind facility property to facilities and property placed in service in 2013. The proposal would also extend the section 1603 program to all otherwise qualifying property placed in service in 2012 (including property on which construction begins in 2012). For property that is placed in service after 2012, the proposal would replace the payment under the section 1603 program with a refundable tax credit administered by the Internal Revenue Service. The credit would be allowed with respect to property placed in service in 2013 (in the case of property, including wind facility property, that is part of a facility eligible for the renewable electricity production tax credit) and for property placed in service during the period 2013-2016 (in the case of any other energy property). The refundable tax credit would be available for property on which construction begins during the period 2009-2013. Qualification requirements for the refundable credit would be the same (except for the effective date provisions) as the qualification requirements currently applicable under the section 1603 program.

3. Additional energy-related tax initiatives

The President's FY 2013 Budget proposes a number of other tax initiatives that will help spur the development of America's renewable energy potential, including the following:

- A proposal to focus the 9-percent deduction for domestic production activities more narrowly on manufacturing activities. The savings would be invested in a two-tier increase in the deduction, with the larger increase (to approximately 18 percent) going to manufacturers of advanced technology property, including renewable energy property.
- A proposal to make permanent an expanded research and experimentation credit. This change would contribute to the domestic development of cutting-edge renewable energy technologies.
- Making advanced vehicles more affordable by expanding the tax credit for electric vehicles to a broader range of advanced vehicle technologies, making the credit scalable based on performance up to a maximum cap of \$10,000, making the credit available to

dealers so it can be provided to consumers as a point-of-sale rebate, and replacing the per-manufacturer cap with a phase-out of the credit over time.

- Providing a tax credit for 50 percent of the incremental cost (relative to the cost of a comparable diesel or gasoline vehicle) of a dedicated alternative-fuel truck, including one powered by natural gas or electricity. The credit would be allowed for a five-year period, with a phase-down in the last year of the period.
- Converting the existing deduction for energy efficient commercial buildings into a more valuable tax credit, making the credit scalable (from \$0.60 per square foot to \$1.80 per square foot) depending on the energy efficiency achieved, specifying prescriptive standards that can be used to qualify for the credit (in lieu of the whole-building auditing, modeling, and simulation required under current law), and allowing the credit to benefit a real estate investment trust (REIT) or its shareholders.

4. *Extend expiring provisions*

The Budget proposes to extend through 2013, without other changes, a number of tax provisions that either have expired or are scheduled to expire at the end of 2012. The following energy incentives are included in the extension proposal:

- *Incentives for biodiesel and renewable diesel.* A \$1.00-per-gallon incentive for biodiesel and renewable diesel is provided as an income tax credit, an excise tax credit, or a refundable payment. In addition, a \$0.10-per-gallon income tax credit is available for small producers. The incentives expired at the end of 2011.
- *Incentives for alternative fuels.* A \$0.50-per-gallon (or gasoline gallon equivalent) excise tax credit or refundable payment is provided for alternative fuels such as liquefied hydrogen, natural gas fuels, liquefied petroleum gas, liquid fuels derived from coal, and liquid fuels derived from biomass. The incentives expired at the end of 2011 for fuels other than liquefied hydrogen.
- *Incentives for cellulosic biofuel.* A \$1.01-per-gallon incentive for cellulosic biofuel is provided as an income tax credit. In addition, 50-percent bonus depreciation is allowed for plants that produce cellulosic biofuel in the year they are placed in service. The incentives expire at the end of 2012.
- *Tax credits for alternative fuel refueling property.* A 50-percent income tax credit is provided for alternative fuel (including electricity) refueling property, subject to a \$30,000 cap for depreciable property and a \$1,000 cap for nonbusiness property. The credit expired at the end of 2011 except for property relating to hydrogen.
- *Tax credits for energy efficient new homes.* A \$2,000 dollar income tax credit is allowed for the construction of an energy efficient home (\$1,000 in the case of a manufactured home). The credit expired at the end of 2011.
- *Tax credits for energy efficiency improvements to existing homes.* A 10-percent income tax credit is allowed for various energy-efficient home improvements (improvements to the building envelope and the installation of energy-efficient heating and cooling equipment). The aggregate credit is limited to \$500. The credit expired at the end of 2011.
- *Tax credits for energy efficient appliances.* A tax credit ranging from \$25 to \$225 is allowed to manufacturers of energy efficient dishwashers, clothes washers, and

refrigerators. The credit is limited (except in the case of refrigerators) to \$25 million per manufacturer and is further limited for a taxable year (including in the case of refrigerators) to 4 percent of average gross receipts for the preceding three years. The credit expired at the end of 2011.

- *Tax credit for plug-in hybrid conversions.* A 10-percent credit (up to \$4,000) is allowed for the cost of converting a used vehicle into a plug-in electric drive motor vehicle. The credit expired at the end of 2011.
- *Deferral of gain on sales to implement electric restructuring policy.* Utilities selling transmission facilities to implement federal or state electric restructuring policy are permitted to report the gain over an 8-year period rather than in the year of sale. This treatment expired at the end of 2011.

Implementation of Section 1603 and 48C Programs

Section 1603

The section 1603 program is administered within the Treasury Department by the Office of the Fiscal Assistant Secretary (OFAS). Because the program incorporates many tax concepts, technical assistance is provided by the Office of Tax Policy in the Treasury Department, the Internal Revenue Service Office of Chief Counsel, and other offices as necessary. In addition, the Treasury Department has entered into an inter-agency agreement with the Department of Energy (DOE) so that Treasury may utilize, as necessary, DOE's engineering, scientific, and other expertise when reviewing applications.

Section 1603 is not a discretionary program, and Treasury is required to make payments to all eligible applicants. Application reviews are focused on determining whether the statutorily mandated eligibility criteria have been met and whether the amount claimed has been appropriately calculated. Recipients are required to make annual reports on the use of the property for a period of five years after receipt of the payment. If the property ceases to meet the eligibility criteria during the five-year period, part or all of the payment will be recaptured.

Section 48C

Unlike section 1603, implementation of section 48C is largely complete. Section 48C also differs from section 1603 in that section 48C is a discretionary program that authorized the Treasury Department to allocate \$2.3 billion dollars in tax credits among advanced energy projects. In addition, awards were limited to projects that had a reasonable expectation of commercial viability. Within this class of projects, Treasury, in consultation with DOE, allocated the limited supply of credits using specified selection criteria including commercial viability, job creation, pollution and greenhouse gas reduction, technological innovation, lowest cost, and shortest completion time.

Because section 48C is a tax provision, the section 48C program is administered within the Treasury Department by the Internal Revenue Service. As in the case of section 1603, the Internal Revenue Service entered into an inter-agency agreement with DOE that enabled the Internal Revenue Service to draw on the expertise of the Office of Energy Efficiency and

Renewable Energy (EERE). During the review process, EERE considered more than 500 applications and, at the conclusion of the review, ranked the projects in descending order of priority. The tax credits were awarded to taxpayers based on this ranking until the \$2.3 billion in available credits was fully allocated.

Based on the experience gained in the 2009 review process, the IRS and EERE are confident that any additional credits authorized by Congress could be quickly and efficiently allocated.

Conclusion

Mr. Chairmen, this concludes my prepared testimony. I will be pleased to answer any questions you or other members of the Committee may have.

APPENDIX: GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2013 REVENUE PROPOSALS RELATED TO ENERGY²

PROVIDE ADDITIONAL TAX CREDITS FOR INVESTMENT IN QUALIFIED PROPERTY USED IN A QUALIFYING ADVANCED ENERGY MANUFACTURING PROJECT

Current Law

A 30-percent tax credit is provided for investments in eligible property used in a qualifying advanced energy project. A qualifying advanced energy project is a project that re-equips, expands, or establishes a manufacturing facility for the production of: (1) property designed to produce energy from renewable resources; (2) fuel cells, microturbines, or an energy storage system for use with electric or hybrid-electric vehicles; (3) electric grids to support the transmission, including storage, of intermittent sources of renewable energy; (4) property designed to capture and sequester carbon dioxide emissions; (5) property designed to refine or blend renewable fuels or to produce energy conservation technologies; (6) electric drive motor vehicles that qualify for tax credits or components designed for use with such vehicles; and (7) other advanced energy property designed to reduce greenhouse gas emissions.

Eligible property is property: (1) that is necessary for the production of the property listed above; (2) that is tangible personal property or other tangible property (not including a building and its structural components) that is used as an integral part of a qualifying facility; and (3) with respect to which depreciation (or amortization in lieu of depreciation) is allowable.

Under the American Recovery and Reinvestment Act of 2009 (ARRA), total credits were limited to \$2.3 billion, and the Treasury Department, in consultation with the Department of Energy, was required to establish a program to consider and award certifications for qualified investments eligible for credits within 180 days of the date of enactment of ARRA. Credits may be allocated only to projects where there is a reasonable expectation of commercial viability. In addition, consideration must be given to which projects: (1) will provide the greatest domestic job creation; (2) will have the greatest net impact in avoiding or reducing air pollutants or greenhouse gas emissions; (3) have the greatest potential for technological innovation and commercial deployment; (4) have the lowest levelized cost of generated or stored energy, or of measured reduction in energy consumption or greenhouse gas emission; and (5) have the shortest completion time. Guidance under current law requires taxpayers to apply for the credit with respect to their entire qualified investment in a project.

Applications for certification under the program may be made only during the two-year period beginning on the date the program is established. An applicant that is allocated credits must provide evidence that the requirements of the certification have been met within one year of the

² The complete set of the General Explanations of the Administration's Fiscal Year 2013 Revenue Proposals can be found on Treasury's website here: <http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2013.pdf>. The relevant energy-related proposals are included in this Appendix.

date of acceptance of the application and must place the property in service within three years from the date of the issuance of the certification.

Reasons for Change

The \$2.3 billion cap on the credit has resulted in the funding of less than one-third of the technically acceptable applications that have been received. Rather than turning down worthy projects that could be deployed quickly to create jobs and support economic activity, the program – which has proven successful in leveraging private investment in building and equipping factories that manufacture clean energy products in America – should be expanded. An additional \$5 billion in credits would support nearly \$17 billion in total capital investment, creating tens of thousands of new construction and manufacturing jobs. Because there is already an existing pipeline of worthy projects and substantial interest in this area, the additional credit can be deployed quickly to create jobs and support economic activity.

Proposal

The proposal would authorize an additional \$5 billion of credits for investments in eligible property used in a qualifying advanced energy manufacturing project. Taxpayers would be able to apply for a credit with respect to part or all of their qualified investment. If a taxpayer applies for a credit with respect to only part of the qualified investment in the project, the taxpayer's increased cost sharing and the project's reduced revenue cost to the government would be taken into account in determining whether to allocate credits to the project.

Applications for the additional credits would be made during the two-year period beginning on the date on which the additional authorization is enacted. As under current law, applicants that are allocated the additional credits must provide evidence that the requirements of the certification have been met within one year of the date of acceptance of the application and must place the property in service within three years from the date of the issuance of the certification.

The change would be effective on the date of enactment.

EXTEND AND MODIFY CERTAIN ENERGY INCENTIVES

Current Law

The general business tax credit includes a production tax credit for wind facilities placed in service in 2012 and certain other renewable energy facilities placed in service before 2014 (the renewable electricity production tax credit). The general business credit also includes an investment tax credit for energy property. Energy property is (1) property that is part of a facility that, but for the election to claim an investment tax credit, would qualify for the renewable electricity production tax credit and (2) certain other listed property (including solar energy property).

The Secretary of the Treasury is required to make grants to persons that place in service property that, but for the receipt of the grant, would be energy property qualifying for the investment tax

credit. In general, the grant is 30 percent of the basis on which the investment tax credit could be claimed. For qualified microturbine, combined heat and power systems, and geothermal heat pump property, the grant is 10 percent of such basis. If a grant is paid with respect to any property, no renewable electricity production tax credit or investment tax credit is allowed with respect to that property.

The grant was available for property that was originally placed in service in 2009, 2010, and 2011. For property placed in service after 2011, the grant is available only if construction of the property began in 2009, 2010, or 2011, and the property is placed in service before 2013 (in the case of wind facility property), 2014 (in the case of other property that is part of a facility that could, but for the receipt of the grant, qualify for the renewable electricity production tax credit), or 2017 (in the case of any other energy property).

Reasons for Change

Investments in property qualifying for the renewable electricity production tax credit and the investment tax credit for energy property further the Administration's policy of supporting a clean energy economy, reducing our reliance on oil, and cutting carbon pollution. The extension of incentives for these investments is necessary to the continued success of that policy. The administration of the incentives could be improved, however, if they were delivered entirely through the Internal Revenue Code by substituting a refundable tax credit for the Treasury grant program.

Proposal

The proposal would extend the production tax credit for wind facilities and the investment tax credit for wind facility property to facilities and property placed in service in 2013. The proposal would also extend the Treasury grant program to all otherwise qualifying property placed in service in 2012 (including property on which construction begins in 2012). For property that is placed in service after 2012, the proposal would replace the Treasury grant with a refundable tax credit administered by the Internal Revenue Service. The refundable tax credit would be available for property on which construction begins in 2009, 2010, 2011, 2012, or 2013. The credit would be allowed with respect to property placed in service in 2013 (in the case of property, including wind facility property, that is part of a facility eligible for the renewable electricity production tax credit) and for property placed in service in 2013, 2014, 2015, or 2016 (in the case of any other energy property). Qualification requirements for the refundable credit would be the same (except for the effective date provisions) as the qualification requirements currently applicable under the Treasury grant program.

TARGET THE DOMESTIC PRODUCTION DEDUCTION TO DOMESTIC MANUFACTURING ACTIVITIES AND DOUBLE THE DEDUCTION FOR ADVANCED MANUFACTURING ACTIVITIES

Current Law

Current law allows a deduction to taxpayers that generate qualified production activities income. Such income is generally calculated as a taxpayer's domestic production gross receipts (DPGR)

less the cost of goods sold and other expenses, losses, or deductions attributable to such receipts. DPGR are those gross receipts derived from any lease, rental, license, sale, exchange, or other disposition of (1) qualifying production property (tangible personal property, computer software, and sound recordings) manufactured, produced, grown, or extracted by the taxpayer in whole or in significant part within the United States; (2) any qualified film produced by the taxpayer (where not less than 50 percent of the total compensation is for labor services performed in the United States); or (3) electricity, natural gas, or potable water produced by the taxpayer in the United States. DPGR also include gross receipts derived from the construction of real property performed in the United States, including receipts derived from the conduct of related engineering or architectural services.

The domestic production deduction is generally equal to nine percent of the taxpayer's qualified production activities income (or of its taxable income, computed before the deduction, if less) for the taxable year. It is computed at a 6 percent rate for income attributable to the production, refining, processing, transportation, or distribution of oil, gas, or any primary product thereof. The deduction may not exceed 50 percent of wages (including amounts of elective deferrals and deferred compensation) paid by the taxpayer for the taxable year that are attributable to DPGR.

Reasons for Change

The current domestic production deduction applies to a broad range of activities beyond core manufacturing activities. Broadening the income tax base by narrowing the scope of the domestic production deduction would allow an increased deduction rate for the activities remaining subject to the provision, and would allow for an even greater incentive for the manufacture of certain advanced technology property.

Proposal

The proposal would limit the extent to which the domestic production deduction is allowed with respect to nonmanufacturing activities by excluding from the definition of DPGR any gross receipts derived from sources such as the production of oil and gas, the production of coal and other hard mineral fossil fuels, and certain other nonmanufacturing activities. Additional revenue obtained from this retargeting would be used to increase the general deduction percentage and to fund an increase of the deduction rate for activities involving the manufacture of certain advanced technology property to approximately 18 percent. The proposal would be roughly revenue neutral over the ten-year budget window.

The proposal would be effective for taxable years beginning after December 31, 2012.

ENHANCE AND MAKE PERMANENT THE RESEARCH AND EXPERIMENTATION (R&E) TAX CREDIT

Current Law

The R&E tax credit is 20 percent of qualified research expenses above a base amount. The base amount is the product of the taxpayer's "fixed base percentage" and the average of the taxpayer's gross receipts for the four preceding years. The taxpayer's fixed base percentage generally is the ratio of its research expenses to gross receipts for the 1984-88 period. The base amount cannot be less than 50 percent of the taxpayer's qualified research expenses for the taxable year.

Taxpayers can elect the alternative simplified research credit (ASC), which is equal to 14 percent of qualified research expenses that exceed 50 percent of the average qualified research expenses for the three preceding taxable years. Under the ASC, the rate is reduced to six percent if a taxpayer has no qualified research expenses in any one of the three preceding taxable years. An election to use the ASC applies to all succeeding taxable years unless revoked with the consent of the Secretary.

The R&E tax credit also provides a credit for 20 percent of: (1) basic research payments above a base amount; and (2) all eligible payments to an energy research consortium for energy research.

The R&E tax credit expired on December 31, 2011.

Reasons for Change

The R&E tax credit encourages technological developments that are an important component of economic growth. However, uncertainty about the future availability of the R&E tax credit diminishes the incentive effect of the credit because it is difficult for taxpayers to factor the credit into decisions to invest in research projects that will not be initiated and completed prior to the credit's expiration. To improve the credit's effectiveness, the R&E tax credit should be made permanent.

Currently, a taxpayer must choose between using an outdated formula for calculating the R&E credit that provides a 20-percent credit rate for research spending over a certain base amount related to the business's historical research intensity and the much simpler ASC that provides a 14-percent credit in excess of a base amount based on its recent research spending. Increasing the rate of the ASC to 17 percent would provide an improved incentive to increase research and would make the ASC a more attractive alternative. Because the ASC base is updated annually, the ASC more accurately reflects the business's recent research experience and simplifies the R&E credit's computation.

Proposal

The proposal would make the R&E credit permanent and increase the rate of the ASC from 14 percent to 17 percent, effective after December 31, 2011.

PROVIDE A TAX CREDIT FOR THE PRODUCTION OF ADVANCED TECHNOLOGY VEHICLES

Current Law

A tax credit is allowed for plug-in electric drive motor vehicles. A plug-in electric drive motor vehicle is a vehicle that has at least four wheels, is manufactured for use on public roads, is

treated as a motor vehicle for purposes of title II of the Clean Air Act (that is, is not a low-speed vehicle), has a gross vehicle weight of less than 14,000 pounds, meets certain emissions standards, draws propulsion energy using a traction battery with at least four kilowatt hours of capacity, is capable of being recharged from an external source, and meets certain other requirements. The credit is \$2,500 plus \$417 for each kilowatt hour of battery capacity in excess of four kilowatt hours, up to a maximum credit of \$7,500. The credit phases out for a manufacturer's vehicles over four calendar quarters beginning with the second calendar quarter following the quarter in which 200,000 of the manufacturer's credit-eligible vehicles have been sold. The credit is generally allowed to the taxpayer that places the vehicle in service (including a person placing the vehicle in service as a lessor). In the case of a vehicle used by a tax-exempt or governmental entity, however, the credit is allowed to the person selling the vehicle to the tax-exempt or governmental entity, but only if the seller clearly discloses the amount of the credit to the purchaser.

Reasons for Change

In 2008, the President set a goal of putting 1 million advanced technology vehicles on the road by 2015 – which would reduce dependence on foreign oil and lead to a reduction in oil consumption of about 750 million barrels through 2030. To help achieve that goal, the President is proposing increased investment in R&D and a competitive program to encourage communities to invest in the advanced vehicle infrastructure, address the regulatory barriers, and provide the local incentives to achieve deployment at critical mass. The President is also proposing a transformation of the existing tax credit for plug-in electric drive motor vehicles into one that is allowed for a wider range of advanced technologies and that is allowed generally to the seller.

Making the credit available to a wider range of technologies, removing the cap placed on the number of vehicles per manufacturer that can receive the credit, and allowing for a scalable credit up to a maximum of \$10,000 will help increase production of advanced vehicles that diversify our fuel use and bring down the cost of producing such vehicles. Moving eligibility for the credit from the purchaser to the person that sells or finances the sale of the vehicle to the ultimate owner would enable the seller or person financing the sale to offer a point-of-sale rebate to consumers. Disclosure requirements, similar to those currently applicable in the case of sales to tax-exempt and governmental entities, would help ensure that the benefit of the credit is passed on to consumers. Shifting the process of claiming the credit from a large number of individual consumers to a relatively small number of business entities would also simplify tax preparation for individuals and reduce the potential for taxpayer error.

Proposal

The proposal would replace the credit for plug-in electric drive motor vehicles with a credit for advanced technology vehicles. The credit would be available for a vehicle that meets the following criteria: (1) the vehicle operates primarily on an alternative to petroleum; (2) as of the January 1, 2012, there are few vehicles in operation in the U.S. using the same technology as such vehicle; and (3) the technology used by the vehicle exceeds the footprint based target miles per gallon gasoline equivalent (MPGe) by at least 25 percent. The Secretary of the Treasury, in consultation with the Secretary of Energy, will determine what constitutes the same technology for this purpose. The credit would be limited to vehicles that weigh no more than 14,000 pounds and are treated as motor vehicles for purposes of title II of the Clean Air Act. In general, the

credit would be the product of \$5,000 and 100 and the amount by which the vehicle's footprint gallons per mile exceeds its gallons per mile, but would be capped at \$10,000 (\$7,500 for vehicles with an MSRP above \$45,000). The credit for a battery-powered vehicle would be determined under current law rules for the credit for plug-in electric drive motor vehicles if that computation results in a greater credit. The credit would be allowed to the person that sold the vehicle to the person placing the vehicle in service (or, at the election of the seller, to the person financing the sale), but only if the amount of the credit is disclosed to the purchaser.

The credit would be allowed for vehicles placed in service after the date of enactment and before January 1, 2020. The credit would be limited to 75 percent of the otherwise allowable amount for vehicles placed in service in 2017, to 50 percent of such amount for vehicles placed in service in 2018, and to 25 percent of such amount for vehicles placed in service in 2019.

PROVIDE A TAX CREDIT FOR MEDIUM- AND HEAVY-DUTY ALTERNATIVE-FUEL COMMERCIAL VEHICLES

Current Law

A tax credit is allowed for fuel-cell vehicles purchased before 2015. The credit is \$20,000 for vehicles weighing more than 14,000 pounds but not more than 26,000 pounds and \$40,000 for vehicles weighing more than 26,000 pounds. There is no other tax incentive for vehicles weighing more than 14,000 pounds.

Reasons for Change

Currently, medium- and heavy-duty trucks consume more than two million barrels of oil every day and account for 20 percent of greenhouse gas emissions related to transportation. Most of these vehicles are powered by diesel fuel. Alternative-fuel vehicles have the potential to reduce petroleum consumption and greenhouse gas emissions. A tax credit would encourage the purchase of such vehicles and the development of a commercially viable manufacturing base for alternative-fuel medium and heavy-duty vehicles.

Proposal

The proposal would allow a tax credit for dedicated alternative-fuel vehicles weighing more than 14,000 pounds. The credit would be equal to 50 percent of the incremental cost of such vehicles compared to the cost of a comparable diesel or gasoline vehicle. The credit would be limited to \$25,000 for vehicles weighing up to 26,000 pounds and \$40,000 for vehicles weighing more than 26,000 pounds. In the case of fuel-cell vehicles, the proposed credit would be reduced by the amount of the credit allowed with respect to the vehicle under current law. The credit would be allowed to the person placing the vehicle in service or, in the case of a vehicle placed in service by a tax-exempt or governmental entity, to the person that sold the vehicle to such entity (or, at the election of the seller, to the person financing the sale), but only if the amount of the credit is disclosed to the purchaser.

The credit would be allowed for vehicles placed in service after December 31, 2012, and before January 1, 2019. For vehicles placed in service in calendar year 2018, the credit would be limited to 50 percent of the otherwise allowable amount.

PROVIDE TAX CREDIT FOR ENERGY-EFFICIENT COMMERCIAL BUILDING PROPERTY EXPENDITURES IN PLACE OF EXISTING TAX DEDUCTION

Current Law

Taxpayers are allowed to deduct expenditures for energy efficient commercial building property. Energy efficient commercial building property is defined as property that (1) is installed on or in any building that is located in the United States and is within the scope of Standard 90.1-2001, (2) is installed as part of (i) the interior lighting systems, (ii) the heating, cooling, ventilation, and hot water systems, or (iii) the building envelope, (3) is certified as being installed as part of a plan designed to reduce the total annual energy and power costs with respect to the interior lighting, heating, cooling, ventilation, and hot water systems of the building by 50 percent or more in comparison to a reference building that meets the minimum requirements of Standard 90.1-2001, and (4) with respect to which depreciation (or amortization in lieu of depreciation) is allowable. Standard 90.1-2001, as referred to here, is Standard 90.1-2001 of the American Society of Heating, Refrigerating, and Air Conditioning Engineers and the Illuminating Engineering Society of North America (ASHRAE/IESNA) as in effect on April 2, 2003 – a nationally accepted building energy code that has been adopted by local and state jurisdictions throughout the United States. The deduction with respect to a building is limited to \$1.80 per square foot.

In the case of a building that does not achieve a 50-percent energy savings, a partial deduction is allowed with respect to each separate building system (interior lighting; heating, cooling, ventilation, and hot water; and building envelope) that meets the system-specific energy-savings target prescribed by the Secretary of the Treasury. The applicable system-specific savings targets are those that would result in a total annual energy savings with respect to the whole building of 50 percent, if each of the separate systems met the system-specific target. The maximum allowable deduction for each of the separate systems is \$0.60 per square foot.

The deduction is allowed in the year in which the property is placed in service. If the energy efficient commercial building property expenditures are made by a public entity, the deduction may be allocated under regulations to the person primarily responsible for designing the property. The deduction applies to property placed in service on or before December 31, 2013.

Reasons for Change

The President has called for a new Better Buildings Initiative that would over 10 years reduce energy usage in commercial buildings by 20 percent. This initiative would catalyze private sector investment in upgrading the efficiency of commercial buildings. Changing the current tax deduction for energy efficient commercial building property to a tax credit and allowing a partial credit for achieving less stringent efficiency standards would encourage private sector investments in energy efficiency improvements. In addition, allowing a credit based on prescriptive efficiency standards would reduce the complexity of the current standards, which require whole-building auditing, modeling, and simulation.

Proposal

The proposal would replace the existing deduction for energy efficient commercial building property with a tax credit equal to the cost of property that is certified as being installed as part of a plan designed to reduce the total annual energy and power costs with respect to the interior lighting, heating, cooling, ventilation, and hot water systems of the building by 20 percent or more in comparison to a reference building which meets the minimum requirements of ASHRAE/IESNA Standard 90.1-2004, as in effect on the date of enactment.

The credit with respect to a building would be limited to \$0.60 per square foot in the case of energy efficient commercial building property designed to reduce the total annual energy and power costs by at least 20 percent but less than 30 percent, to \$0.90 per square foot for qualifying property designed to reduce the total annual energy and power costs by at least 30 percent but less than 50 percent, and to \$1.80 per square foot for qualifying property designed to reduce the total annual energy and power costs by 50 percent or more.

In addition, the proposal would treat property as meeting the 20-, 30-, and 50-percent energy savings requirement if specified prescriptive standards are satisfied. Prescriptive standards would be based on building types (as specified by Standard 90.1-2004) and climate zones (as specified by Standard 90.1-2004).

Special rules would be provided that would allow the credit to benefit a REIT or its shareholders.

The tax credit would be available for property placed in service during calendar year 2013.