RSC Republican Study Committee

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Legislative Bulletin……………………………………..…..February 27, 2008

Contents:

H.R. 5351—Renewable Energy and Energy Conservation Tax Act

Summary of the Bill Under Consideration Today:

Total Number of New Government Programs: 0

Total Cost of Discretionary Authorizations: Unknown but not a large amount

Effect on Revenue: Net $86 million increase over eleven years

Total Change in Mandatory Spending: $0

Total New State & Local Government Mandates: 0

Total New Private Sector Mandates: 2

Number of *Bills* Without Committee Reports: 1

Number of *Reported* Bills that Don't Cite Specific Clauses of Constitutional Authority: 0

H.R. 5351— Renewable Energy and Energy Conservation Tax Act (*Rangel, D-NY*)

SEE CONSERVATIVE CONCERNS ON PAGE 2.

Order of Business: The bill is reportedly scheduled to be considered on Wednesday, February 27, 2008, subject to a likely closed rule (allowing no amendments). The rule will be summarized in a separate RSC document.

NOTE: Most of the provisions in this legislation are identical or similar to what was included in the House-passed version of H.R. 2776 from August 2007, which the House passed by a mostly

party-line vote of 221-189, as well as in the version of H.R. 6 that the House passed in December 2007 by a mostly party-line vote of 235-181. (The Senate removed the tax language from H.R. 6 and sent it back to the House, which accepted the bill as amended.)

To read the RSC Legislative Bulletin for H.R. 2776 from August 2007, visit this webpage: http://www.house.gov/hensarling/rsc/doc/LB_080307_energytax.doc. To read the RSC Legislative Bulletin for H.R. 6 from early December (before the Senate stripped out the tax language), visit this webpage:
http://www.house.gov/hensarling/rsc/doc/lb_120607_energy.doc.

Possible Conservative Concerns: Some conservatives may be concerned about the following provisions in this bill:

- **$17.71 billion in tax increases** on certain energy producers over eleven years;
- Disincentives for domestic energy production and investment, making foreign energy investment and reliance more attractive;
- The apparent motivation behind this bill that it is the federal government's responsibility to determine which American companies' profits are too high and to subsequently try to reduce them;
- The application of Davis-Bacon prevailing wage requirements to all tax-credit bonds;
- The violation of the allowable threshold for the Unfunded Mandates Reform Act (see mandates section on page 8 below);
- The use of a corporate estimated tax payment shift (to meet Washington's arbitrary budget scoring rules) that has real-world implications requiring the surrender of more cash to the federal government earlier than otherwise necessary; and
- The termination of the New York Liberty Zone program in such a way that yields a $2 billion windfall for New York for any transportation infrastructure project. This provision might be construed as an earmark for New York City.

Some conservatives may also be concerned about taking a financial shot at today's energy producers at a time when crude oil, the price of which makes up more than half of the price of a gallon of gas at the pump (according to the American Petroleum Institute), is at a record high and when Congress has failed to send to the President legislation that would allow energy producers to find new resources in new areas (like the Outer Continental Shelf) or to build or expand refineries.

Summary: H.R. 5351 would increase taxes on certain energy producers and provide a variety of tax incentives for producing renewable energy and for conserving energy, as follows (by title):

Title I—Production Incentives
This title would save taxpayers $8.46 billion over eleven years.

- Extends the renewable energy tax credit (2.0 cents per kilowatt/hour for electricity generated from wind, biomass, geothermal, solar, landfill gas, trash combustion, etc., indexed for inflation) for an additional three years, from the end of 2008 through the end of 2011.

- Allows the tax credits for refined coal and Indian coal to expire at the end of 2008.

- Adds marine and hydrokinetic renewables as a qualifying energy source under the renewable energy tax credit above. Marine renewables include electricity produced from waves, tides, currents, rivers, lakes, streams, irrigation systems, canals, and ocean thermal energy conversion.

- Extends the 30% investment tax credit for solar and fuel cell property for commercial use from the end of 2008 to the end of 2016, and permits the credit to be claimed against the corporate Alternative Minimum Tax (AMT).

- Increases the solar/fuel cell credit limitation for fuels cells from $500 to $1,500 for each .5 kilowatt of capacity and repeals the prohibition against public utilities claiming the credit.

- Creates $2 billion in new clean renewable energy bonds, 100% of the available project proceeds of which would be used for capital expenditures incurred by public power providers or cooperative electric companies to construct one or more qualified renewable energy facilities (using one or more of the fuels listed above). The bill provides details for calculating the tax credit generated from the purchase of such bonds. In addition, the bonds would be tradable and could not be issued by state and local governments. **Davis-Bacon prevailing wage standards would apply to projects funded by these bonds.**

- Extends through the end of 2014 the residential solar and fuel cell credit and increases the $2,000-per-taxpayer cap to $4,000. This credit could also be claimed for residential small wind equipment and geothermal heat pumps.

- Allows the solar and fuel cell credit to be taken against the AMT.

Title II—Conservation

This title would save taxpayers $9.10 billion over eleven years.

- Creates a new personal or business tax credit up to $6,000 for plug-in hybrid automobiles (based on battery capacity).

- Phases out the credit applicable to vehicles that have more than 60,000 of them sold in the U.S. (total).

- Extends the alternative fuel vehicle refueling property credit (e.g. ethanol and biodiesel gas station pumps) for one year, from the end of 2009 to the end of 2010. Increases the credit from 30% to 50% of the property value and increases the total taxpayer annual credit cap from $30,000 to $50,000.

- Expands the definition of automobile that would be subject to a longer (i.e. five-year) depreciation schedule to any new vehicle weighing up to 14,000 pounds (current law is

6,000 pounds). The bill also makes certain exceptions for farming vehicles, taxis, ambulances, vehicles with intended room for more than nine people behind the driver's seat, pick-ups with a five-foot bed or greater, and vehicles substantially used to transfer, move, or deliver equipment, inventory, or supplies.

- Extends the biodiesel credit and the renewable diesel credit for two years, from the end of 2008 to the end of 2010. Makes the renewable diesel credit technology-neutral and requires that renewable diesel be vehicle-quality fuel.

- Stipulates that the per-gallon tax incentives for biodiesel, renewable diesel, and alternative fuels are incentives for the production of fuels in the United States. The bill would also provide that the per-gallon tax incentives for alcohol fuels, biodiesel, renewable diesel, and alternative fuels are limited to fuels that are produced for consumption in the United States (applicable to fuel produced, sold, and used, after December 31, 2008). *Note: This provision would yield a* ***$68 million tax increase*** *on oil and gas companies over three years.*

- Creates a new 50-cents-per-gallon tax credit for producers of cellulosic alcohol (i.e. cellulosic ethanol). The Republican staff of the Ways & Means Committee notes that this credit would be in addition to the general ethanol credit of 51 cents per gallon.

- Makes permanent the income exclusion (up to $20 per month) for bicycle commuting fringe benefits paid by an employer.

- Terminates the remaining portions of the New York Liberty Zone tax incentives program (implemented to encourage business investment in lower Manhattan)—the first-year 30% depreciation allowance and the additional section 179 expensing in the case of nonresidential real property and residential rental property.

- Requires the federal government to surrender its claim to about $2 billion in federal income taxes withheld on New York City and state employees as part of the Liberty Zone program. These surrendered funds could be used by New York for any transportation infrastructure project, including highways, mass transit, railroads, airports, ports, waterways, etc. This provision might be construed as an earmark for New York City.

- Creates $3.6 billion of new tax-credit bonds to be used for qualified energy conservation purposes (as detailed in the bill to include such things as capital expenditures for reducing energy consumption in public buildings by 20%, research grants for carbon capture technologies, mass commuting facilities, projects for "green" building technologies, and pubic education campaigns to promote energy efficiency). States and localities would have to issue the bonds, distributed to them on a per-capita basis (plus a suballocation for large cities and counties). The bonds would be tradable and **would be subject to Davis-Bacon requirements.**

- Extends the $300 credit for non-business energy property (i.e. residential energy-efficiency improvements to existing homes) for two years—to the end of 2009—and adds residential biomass-fuel stoves heaters to claimable property.

- Extends the efficient commercial building tax deduction from the end of 2008 through the end of 2013. (The current deduction is $1.80 per square foot of the property for which expenditures are made to reduce the energy consumption of a commercial building by 50%.).

- Extends and modifies (as detailed in the bill) the manufacturer's tax credit for the production of energy efficient dishwashers, clothes washers, and refrigerators—and provides new tax credits for energy efficient dehumidifiers. Limits a manufacturer's total claim of credits under this section to $75 million per year.

- Shortens the depreciable life of qualifying "smart meters" installed by a utility from 20 years to 5 years, and requires that a qualifying meter measure and record electricity usage on a time-differentiated basis at least 24 times per day, while providing real-time price and usage data to customers and to the electricity supplier.

Title III—Revenue Provisions

According to the Joint Committee on Taxation, Title III of this bill includes $17.65 billion in tax increases on energy producers over eleven years.

- Denies a corporate tax deduction for income attributable to the production, refining, processing, transportation, and distribution of oil, natural gas, or any primary product thereof, beginning in 2009, for the five largest oil and gas companies. For any other (i.e. smaller) oil and gas manufacturing activity that would still qualify for the deduction, the rate would be permanently frozen at 6%, instead of rising to 9%, as scheduled under current law. According to the Joint Committee on Taxation, this provision would amount to a **$13.57 billion tax increase** on oil and gas companies over ten years. *NOTE: This language is the same as in H.R. 6, the Democrat energy-regulation-and-tax-increase bill that passed the House on December 6, 2007.*

- Modifies the method by which oil and gas companies calculate their foreign tax credits, beginning in 2009. Specifically, the provision would require foreign-based income to be reclassified as foreign oil and gas extraction income (FOGEI) for purposes of calculating the foreign tax credit and require "arm's-length" pricing for FOGEI. The Republican staff of the Ways & Means Committee notes that the rules governing FOGEI are more stringent than the general rules governing calculation of foreign tax credits, resulting in a smaller overall foreign tax credit for companies with non-U.S. oil and gas production income. According to the Joint Committee on Taxation, this section would amount to a **$4.08 billion tax increase** on oil and gas companies over eleven years. *NOTE: This language is the same as in H.R. 2776, the Democrat energy-tax-increase bill that passed the House on August 4, 2007.*

- Increases the estimated tax payments that certain corporations must remit to the federal government at the end of fiscal year 2013. Under current law, corporations with assets of at least $1 billion must make estimated tax payments for each quarter of fiscal year 2013 that are 25% of the annual total. H.R. 5351 would require that qualified corporations remit 103% of the estimated payment otherwise due in the fourth quarter of fiscal year 2013. The payment due for the first quarter of fiscal year 2014 would be reduced accordingly so that the corporations pay no net increase in estimated payments in calendar-year (i.e. tax-year) 2013.

  This increase would force applicable companies to increase their estimated payments by about **$1.72 billion** in the last quarter of FY2013 (though they would be offset by a corresponding reduction in the subsequent quarter).

  NOTE: To Washington, this provision is merely a revenue timing shift, a budget gimmick that has been used previously (for FY2012) to comply with the House's PAYGO rules and has no net budget effect over ten years. Without this gimmick, the bill would fail the PAYGO test for the five-year period. But to American companies, this provision has real-world implications requiring the surrender of more cash to the federal government earlier than otherwise necessary and adding further uncertainty to the already-confusing and burdensome task of paying federal taxes.

Title IV—Other Provisions

- Authorizes $1.5 million for the National Academy of Sciences to study and report to Congress on the sections of the tax code that have the largest effects on carbon and other greenhouse gas emissions.

- Directs the Secretary of Treasury, in connection with the Secretary of Agriculture, the Secretary of Energy, and the EPA Administrator, to enter into an agreement with the National Academy of Sciences to analyze current scientific findings to determine current and future potential for biofuels, as well as such matters as the conversion of corn ethanol plants to cellulosic ethanol, and a comparison of corn ethanol against other types of biofuels.

- **Applies Davis-Bacon prevailing wage requirements to all projects funded with the proceeds of any tax-credit, renewable energy bond** (not just the ones specifically referenced in this legislation).

NOTE: H.R. 5351 would NOT extend the research and development tax credit.

Additional Background:

Section 199 Tax Deduction: Current law (26 U.S.C. 199), passed as part of the "FSC-ETI" bill (Public Law 108-357), provides for a (phased-in 9%) corporate tax deduction for most domestic economic manufacturing and production (except retail food sales and the transmission or distribution of electricity, natural gas, or drinkable water). This tax deduction was a replacement

for the extraterritorial income ("ETI") exclusion deemed noncompliant with requirements of the World Trade Organization. This bill would add oil and gas production and distribution as an exception to this deduction so that they could not deduct such expenditures (and thus be subject to a substantial tax increase). This would amount to a multi-billion-dollar tax increase on oil and gas companies that could yield higher energy prices for consumers. Disincentives for domestic energy production and investment naturally make foreign energy investment and reliance more attractive.

Democrats have cited increasing oil-industry profits as the prime motivation behind this legislation. Thus, Democrats believe it is the federal government's responsibility to determine which American companies' profits are too high and to subsequently try to reduce them. Furthermore, Americans for Tax Reform has noted that, "Almost all large oil and gas companies are publicly-traded entities, whose shares are owned by millions of investors through their 401(k) plans, retirement plans and pension funds. Taxing away the earnings of those companies negatively impacts the ability of hard-working Americans to achieve a more financially secure future."

On January 16, 2007, the *Wall Street Journal* editorialized about H.R. 6 containing the Section 199 carve-out for oil and gas that "the biggest winner may be OPEC." On the same day, even the *New York Times* cast doubt on the repeal of tax incentives in H.R. 6: "Fair enough, but that's not an energy policy."

According to the American Petroleum Institute (API), citing information from the Department of Energy's Energy Information Administration (EIA), in 2006, the top 27 energy producing companies accounted for about 44% of the total U.S. crude oil and natural gas production, and 81% of U.S. refining capacity. In that same year, these companies paid about $81.5 billion in income taxes (**an 82% increase in just two years**), resulting in an overall effective tax rate of 37%— more than the top U.S. corporate income tax rate of 35%.

Additional Information on Renewables: According to the Department of Energy's Energy Information Administration (EIA), all renewable energy sources provide 3.1 % of our current energy supply. Wind power produces 0.1% of our energy, and solar provides less than 0.01% of our energy supply, while ethanol provides 1.2% of our transportation fuel, and hydrogen fuel cells are not currently in mass production.

The EIA reports that hydrogen fuel requires large amounts of energy to produce, must be stored near absolute zero, and is highly explosive.

The EIA also reports that solar power requires tremendous amounts of space to produce (6,750 acres to produce the same amount of power that a conventional gas-fired 500 megawatt plant produces on 55 acres) and requires duplicate conventional capacity for when the sun is not shining. The EIA projects that solar power will supply 0.6% of the country's total energy supply by the year 2030.

Wind power also has a space problem. Windmills require 29,250 acres to produce the same amount of power that a conventional gas-fired 500 megawatt plant produces on 55 acres and

requires duplicate conventional capacity for when the wind isn't blowing. The EIA projects that wind will supply 0.5% of the country's total energy supply by the year 2030.

The EIA projects that all biomass will supply 0.6% of the country's total energy supply by the year 2030.

Source for much of the above: http://www.eia.doe.gov/oiaf/aeo/index.html. Additional information was provided by Winningreen, LLC.

Despite the uncertainties of renewable fuels, private investment in them has soared. On January 16, 2007, the *Wall Street Journal* noted that, "The research firm New Energy Finance has found that between 2004 and 2006 investment in alternative energy doubled to $63 billion. Venture capital funding of green-energy technologies has quadrupled since 1998."

Committee Action: On February 12, 2008, the bill was referred to the Ways & Means Committee, which took no subsequent public action on it.

Administration Position: Although a Statement of Administration Policy (SAP) for H.R. 5351 was not available at press time, the Administration will likely oppose this bill, based on past opposition to such bills as H.R. 6 and H.R. 2776.
http://www.whitehouse.gov/omb/legislative/sap/110-1/hr2776sap-r.pdf
http://www.whitehouse.gov/omb/legislative/sap/110-1/hr6sap-h.pdf

Cost to Taxpayers: The Joint Committee on Taxation estimates that this bill would reduce revenues by a net $534 million in FY2008, a net $1.70 billion over the FY2008-FY2012 period, and a net $704.0 million over the FY2008-FY2017 period.

A CBO estimate of the appropriations authorized in this bill is unavailable, though the number (for studies and such) is likely to be relatively low.

Does the Bill Expand the Size and Scope of the Federal Government?: No.

Does the Bill Contain Any New State-Government, Local-Government, or Private-Sector Mandates?: Yes. For H.R. 2776, CBO noted that, "JCT has reviewed the tax provisions of H.R. 2776 and has determined that they contain two private-sector mandates as defined in UMRA: the denial of deduction for income attributable to domestic production of oil, natural gas, or primary products thereof; and the clarification of determination of foreign oil and gas extraction income." CBO notes that the mandates would violate the allowable threshold under the Unfunded Mandates Reform Act (UMRA) ($131 million in 2007, adjusted annually for inflation) in each year beginning in 2009.

Does the Bill Comply with House Rules Regarding Earmarks/Limited Tax Benefits/Limited Tariff Benefits?: A statement in the Congressional Record of February 25, 2008, notes that, "H.R. 5351, the Renewable Energy and Energy Conservation Tax Act of 2008, does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause

9(d), 9(e), or 9(f) of Rule XXI." Note that the bill does contain limited tax *punishments*, since it denies a tax deduction only for the five largest oil and gas companies.

Constitutional Authority: A committee report citing constitutional authority is unavailable.

Outside Organizations: The following organizations have expressed **opposition** to H.R. 5351 (ones with a star are scoring or potentially scoring the bill in their annual ratings of Congress):

- American Conservative Union*
- American Petroleum Institute
- Americans for Prosperity*
- Americans for Tax Reform*
- Competitive Enterprise Institute
- Council for Citizens Against Government Waste*
- FreedomWorks
- Independent Petroleum Association of America
- Koch Industries
- National Association of Manufacturers
- National Petrochemical and Refiners Association
- National Taxpayers Union*
- Natural Gas Supply Association
- Property Rights Alliance
- 60 Plus
- Small Business and Entrepreneurship Council*
- U.S. Oil & Gas Association

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