



UPDATE REPORT

Opportunities for the Energy Industry in The American Recovery and Reinvestment Act of 2009

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The American Recovery and Reinvestment Act (i.e. the Stimulus Act) recently passed by Congress contains an array of energy initiatives that seeks to overhaul the American energy landscape. With a renewed and purposeful focus on energy research and development, climate change, and tax policy, the Act aims to reduce the nation's dependence on foreign oil, increase our renewable energy production and efficiency, accelerate deployment of smart grid technology, and provide funding and support to those involved in tackling the nation's energy challenges.

Energy sector professionals must stay informed of fast-paced industry changes in order to capitalize on opportunities as they present themselves. Now that the Act has been passed, we must focus on the "next steps" of the federal energy agenda and how legislative change may affect businesses.

Research and Development

The majority of funds allocated in the Stimulus Act toward the energy sector involve research and development, as the government seeks to improve our energy independence and efficiency and promote job growth. Incentive programs are far-reaching, from developing a smart energy grid to upgrading the energy efficiency of home appliances. Any business that involves energy use or production could benefit from the Act.

Some of the larger energy projects funded by the Act include:

- \$11 billion for the Smart Grid Investment Program to modernize the electricity grid and build new power lines to transmit clean, renewable energy.
- \$6.3 billion in Local Government Energy Efficiency Grants to help state and local governments make investments in energy efficiency and carbon reduction projects.
- \$6 billion in Renewable Energy Loan Guarantees for renewable energy power generation and transmission projects.
- \$5 billion to help low-income families reduce their energy costs by weatherizing their homes.
- \$4.5 billion for renovations and repairs to federal buildings, focused on increasing energy efficiency and conservation.

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The Act also includes \$2.5 billion for energy efficiency and renewable energy research, development, demonstration, and deployment activities; \$2 billion for the Advanced Battery Grants Program; and \$2 billion for physical sciences research (including high-energy physics, nuclear physics, and fusion energy sciences); and financial support for high-risk, high-payoff research into energy sources and energy efficiency.

On the consumer front, the Act allocates \$250 million to upgrade energy efficiency in HUD-sponsored low-income housing; \$300 million in consumer rebates for buying energy-efficient Energy Star products; and \$400 million to encourage electric vehicle technologies.

Climate Change¹

Now fully in the spotlight, climate change is not only an area of extreme social importance but also an area ripe for development. For businesses involved in addressing climate change, the government wants to help. By injecting unprecedented funds into this area, the Act seeks to generate jobs and ideas that could pay global dividends.

The Act has allocated \$3.4 billion for carbon capture and sequestration technology demonstration projects; \$300 million to help state and local governments purchase efficient alternative fuel vehicles; and \$300 million in grants and loans to state and local governments for projects that reduce diesel emissions. To reduce fuel costs and carbon emissions, heavy investment will be made in technologies to retrofit emission exhaust systems on school buses, replace engines and vehicles, and establish anti-idling programs.

Tax Policy²

The nation's tax policy is becoming more business friendly and is rewarding investments in new energy alternatives. For

those businesses that are already engaged in or are considering alternative energy and efficiency projects, now is a prudent time to invest. An understanding of the tax incentives being offered through the Stimulus Act could help you navigate a strategic business strategy.

The Act authorizes \$1.6 billion in new renewable energy bonds to finance facilities that generate electricity from alternative energy sources. The bond allocation will be subdivided into thirds between qualifying projects of state/local/tribal governments, public power providers, and electric cooperatives. \$2.4 billion in qualified energy conservation bonds has also been established to finance government programs and initiatives designed to reduce greenhouse gas emissions. The bonds may be issued to make loans and grants for capital expenditures to implement green community programs, as well as for programs in which utilities provide ratepayers with energy-efficient property and recoup the costs of that property over an extended period of time.

Renewable Energy and Efficiency Credits

To assist energy-minded companies and investors, the Stimulus Act offers several credits that can be used to offset some of the costs associated with developing energy efficiency.

Under the Act, the Secretary of Treasury may allocate up to \$2.3 billion in Advanced Energy Investment credits as part of a new 30% investment tax credit. Facilities engaged in the manufacture of advanced energy property, including technology for the production and storage of renewable energy, efficient electricity transmission and distribution, and carbon capture and sequestration, will be eligible once certified through a competitive bidding process. An alternative refueling property credit has also been expanded,



which provides a tax credit to businesses (e.g., gas stations) that install alternative fuel pumps. For 2009 and 2010, the Act would increase the 30% alternative refueling property credit for businesses (capped at \$30,000) to 50% (capped at \$50,000). Hydrogen refueling pumps would remain at a 30% credit percentage; however, the cap for hydrogen refueling pumps will be increased to \$200,000.

Modifications to Current Credits

The Act also extends or modifies several energy tax credits already in existence. Clearly, the government is looking at its investment in energy technology as a long-term process that needs to be nurtured through the current economic environment.

One of the most intriguing energy tax modifications found in the Stimulus Act deals with the treatment of Internal Revenue Code § 45, the Renewable Energy Production Tax Credit (the “PTC”). First, the Act extends the availability of the PTC for three years, attempting to end the on-again, off-again cycle that has plagued this program and limited its effectiveness over the years. Qualifying facilities include wind facilities (through December 31, 2012), and certain other facilities such as closed- or open-loop biomass, geothermal, small irrigation, hydropower, landfill gas, waste-to-energy, and marine renewable facilities (through December 31, 2013).

More interestingly, the Act also allows investors in most projects that previously qualified for the PTC to claim a new 30% Business Energy Credit (“BEC”), which is the equivalent to the § 48 Investment Tax Credit (“ITC”).³ Further, the “placed in service” deadline for the BEC extends to December 31, 2014 (December 31, 2013 for wind). Previously, the PTC could be taken over a five-to-ten-year period (ten for wind), while the ITC had to be taken in the year the qualifying project was placed in service (30% credit for solar, fuel cell, small wind property; 10% credit for other

qualifying technologies). Now, most technologies qualifying for the PTC can claim the BEC.

The Treasury provides grants in lieu of the PTC and ITC as long as the project is placed in service before December 31, 2010, or if construction began during 2009 or 2010 and the projects are placed in service before:

- 2013 for wind (30% credit)
- 2014 for biomass, geothermal, landfill gas, waste-to-energy, hydropower, and marine renewables (30% credit)
- 2017 for fuel cell, solar, and small wind (30% credit)
- 2017 for geothermal, microturbine, combined heat and power, and geothermal heat pump property (10% credit).

Developers must choose between the three credits (PTC, ITC and BEC) to determine which provides the most benefit, as only one can be utilized per project. The PTC offers an annual benefit that is dependent on the production of electricity from the Project. The BEC/ITC is an up-front payment that is based on the capital cost of that portion of the project placed in service during the tax year.

The BEC/ITC may be a better financing vehicle for projects with higher capital costs, but for which energy production may be less dependable. The ITC may also be more attractive to lenders who might normally avoid the technology risk inherent in valuing ten years of electric generation. The PTC may be more valuable where capital costs are lower, but the capacity factor for electric generation is high over a longer period of time. The PTC may also be more valuable where the up-front credits are not currently available.

Tax or financial advisors should be consulted to evaluate the benefits of using the various credits to compare their relative net present value, so the developer can choose the most beneficial credit.

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In other key energy related measures, the Act also:

- repeals the subsidized energy financing limitation on the investment tax credit in order to allow businesses and individuals to qualify for the full amount.
- repeals individual dollar caps on certain energy credits, allowing for an uncapped 30% credit for qualified small wind energy property, solar water heating property, small wind energy property, and geothermal heat pumps.
- extends tax credits for qualified energy efficiency improvements to existing homes through 2010 and also increases the amount of the credit from 10% to 30% of the amount incurred by the taxpayer, eliminates property-by-property dollar caps, and provides an aggregate \$1,500 cap on all property qualifying for the credit.
- modifies and increases a tax credit for each qualified plug-in electric drive vehicle placed in service during the taxable year to a base amount of \$2,500 and provides a tax credit for plug-in electric drive conversion kits.

¹The Committee on Appropriations, Summary: American Recovery and Reinvestment Conference Agreement, 2/13/09

²The Senate Finance and the House Ways & Means Committees, Summary: The American Recovery and Reinvestment Act, 2/12/09

³Excluding small irrigation power facilities, refined coal production facilities, and Indian coal production facilities. IRC § 48(a)(5).

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