F I S C A L   I M P A C T   R E P O R T

SPONSOR HTRC **DATE TYPED** 03/18/05 **HB** 121/HTRCS

SHORT TITLE SOLAR-ENERGY RENEWABLE ENERGY TAX CREDITS **SB**

ANALYST Padilla-Jackson

REVENUE

Estimated Revenue		Subsequent Years Impact	Recurring or Non-Rec	Fund Affected
FY06	FY07			
($1,000.0)*	($2,000.0)	($4,000.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

* According to TRD, the state would accrue cost due to foregone tax revenue beginning in FY06, even though the credits cannot be claimed until tax year 2007. This is because the proposal authorizes the payments of a refundable credit for systems installed on or after July 1, 2005. Under full accrual accounting, the state must recognize foregone revenue from a refundable tax credit as soon as the activity has taken place that gives rise to the credit.

Relates to: House Bill 42

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Energy, Minerals & Natural Resources Department (EMNRD)

SUMMARY

Synopsis of Bill

The House Taxation and Revenue Substitute for House Bill 121 proposes various changes to the Renewable Energy Production Tax Credit and introduces the Solar Thermal and Photovoltaic Systems Tax Credit Act.

Renewable Energy Production Tax Credit
The current law provides a $0.01 per kilowatt-hour (kWh) tax credit to a taxpayer that owns a qualified energy generator. House Bill 121 applies the $0.01 per kWh credit specifically to the use of wind or biomass in electricity generation (for the first four hundred thousand megawatt-

hours in the taxable year). The bill increases the credit that applies to electricity generated using solar-light or solar-heat to $0.02 per kWh for the first two hundred thousand megawatt-hours.

The existing statute defines "qualified energy generator" to mean a facility with at least ten megawatt generating capacity located in New Mexico that produces electricity using a qualified energy resource and that sells that electricity to an unrelated person. House Bill 121 lowers the requirement for qualifying facilities to those with at least one megawatt generating capacity.

House Bill 121 makes the renewable energy production tax credit refundable, meaning that if the amount of the tax credit claimed exceeds the tax liability, the excess shall be refunded to the taxpayer. A taxpayer is eligible for the credits for a qualified energy generator placed in commercial operation after January 1, 2007.

Solar Thermal and Photovoltaic Systems Tax Credit Act
House Bill 121 also provides a tax credit against personal or corporate income tax liability for 15 percent of the installation cost of a solar thermal system at a residence in New Mexico, not to exceed $1,500. Additionally, the bill caps the total tax credits provided at $1 million. This tax credit is available on or after January 1, 2006 through December 31, 2015. The taxpayer can rollover any unused portion of the tax credit for three years, or if the person claiming the credit has no tax liability, then the tax credit may be refunded to that person.

Section five of this bill allows an additional tax credit against personal income and corporate income tax liability. The credit for personal income is $3.50 per nameplate direct current wattage of the photovoltaic system provided that: (1) the maximum tax credit shall not exceed $10 thousand; and (2) the total tax credits do not exceed $2 million. The credit for corporate income tax is $1.50 per nameplate direct current wattage of that photovoltaic system, not to exceed $75 thousand per credit and not to exceed a total of $1 million for all credits provided by the department. This tax credit is also allowed on or after January 1, 2006 through December 31, 2015. The taxpayer can rollover any unused portion of the tax credit for three years, or if the person claiming the credit has no tax liability, then the tax credit may be refunded to that person.

The bill defines a "photovoltaic system" to mean a stand-alone or a grid-connected energy system that collects or absorbs sunlight for conversion into electricity. It defines "solar thermal system" to mean an energy system that collects or absorbs solar heat energy for conversion into heat for the purposes of space heating and water heating.

The bill would appropriate $150 thousand from the general fund to EMNRD in FY06 for the purpose of administering the provisions of this act. The bill would appropriate an additional $150 thousand from the general fund to EMNRD in FY06 to provide training to installers, inspectors, and the public on the tax credits allowed pursuant to the act and on installation and operation of solar thermal and photovoltaic systems. Any unencumbered balances remaining at the end of FY06 would revert to the general fund.

The provision of this bill would apply to taxable years beginning on or after January 1, 2005.

<u>Significant Issues</u>

According to EMNRD, the proposed changes to the existing tax credit significantly improve the incentive for renewable energy use in New Mexico, and therefore stimulate economic development, particularly in rural areas of the state. The amendments increase the likelihood of a diverse mix of renewable projects (wind, community-based biomass projects, solar) and serve to accelerate the timing of project development.

According to the Air Quality Bureau, the state is obligated to report every five years to the U.S. Environmental Protection Agency its progress in achieving the renewable energy goal of 10 percent of the regional power needs by 2005 and 20 percent by 2020. They agency believes that implementation of such a bill will help the state achieve these renewable energy goals and better address regional haze in New Mexico's national parks and wilderness areas.

PERFORMANCE IMPLICATIONS

The promotion, development, and implementation of renewable energy programs are key components to EMNRD’s Energy Conservation and Management Division’ strategic plan, which would be supported by this bill.

FISCAL IMPLICATIONS

Solar Thermal and Photovoltaic Systems Tax Credit Act
TRD notes that the impacts of this bill are primarily attributable to the new solar energy tax credits. The maximum total credit amounts of $1 million for solar thermal, $2 million for residential photovoltaic and $1 million for commercial photovoltaic are assumed to apply on an annual basis. Since the credits are refundable, the use would not be limited by the level of tax liabilities. Combined utilization of all the new credits is assumed to be $1 million in tax year 2006, with 50 percent of that amount accruing in FY06. Credits would increase as more people become aware of the availability of the credit.

Renewable Energy Production Tax Credit
TRD notes that the smaller size threshold and increased credit rate for solar power could increase utilization of the renewable energy production tax credit in the near term. The fiscal impacts are limited, however, until the refundability provision takes effect in 2007. In the longer-run, the bill could actually reduce the fiscal impacts of the credit, because it reduces the aggregate amount of power production eligible for the credit. These effects are uncertain because the total credit claims are not likely to exceed the new cap in the bill for a number of years.

ADMINISTRATIVE IMPLICATIONS

The bill would require EMNRD to certify a solar thermal or a photovoltaic systems. EMNRD would also be responsible for adopting and publishing on its website an initial description and requirements no later than August 1, 2005. The bill would require TRD to prescribe application forms for the tax credits allowed no later than December 31, 2006.

According to TRD, the provisions of the bill may be administratively complex for TRD, depending on the rules adopted by the Energy Minerals and Natural Resources Department (“EMNRD”). A new application and claim form would need to be developed. Changes to instructions and publications would be required. Manual review, approval and tracking of the credit claimed and the carry-forward amounts would be required. Audit and compliance procedures must be developed. Depending on the number of claimants for the new credits, the Department may need as many as 1 to 2 FTEs to administer the credits.

OTHER SUBSTANTIVE ISSUES

TRD cautions that the proposed rate of subsidy for solar power generation is approximately half of the average market value of electric power. Electric power is now trading in wholesale markets at prices averaging approximately 4 cents per kilowatt-hour. Thus, the proposed 2-cent per kilowatt-hour credit is equal to 50 percent of the market value of the power.

TECHNICAL ISUES

TRD provided the following comments:

The sections creating the new solar power income tax credits have confusing names. Both individual income and corporate income taxes are included in each section. The sections, however, are named as though each deals with corporate income tax only.

Credit limit provisions:
The amount of each type of credit that may be claimed by a taxpayer is limited. For example, the solar thermal credit is limited to $1,500 per taxpayer for residential installations. It is not clear from the present language whether this limit is to be imposed on an annual basis or over the lifetime of the taxpayer.

Credit cap allocation:
Caps are imposed on the aggregate amount of tax credits allowed under the solar thermal credits ($1 million of both personal and corporate income tax), the residential-photovoltaic credits ($2 million of individual income tax) and other-photovoltaic ($1 million of corporate income tax). The language defining these caps is unclear. The cap in section 4(C) appears to be meant to apply to all of the credits in that section, but the language says it applies to the "subsection." The method of distributing amounts under the new cap – in the event that total claims exceed the cap – is not explained. Language similar to that in the present law renewable energy production tax credit, which assigns to EMNRD the task of allocating capacity under the cap, would make the administration of the caps much clearer. Finally, the language should clarify whether the caps are intended to apply on an annual basis, or be cumulative over time.

Refundability:
The language governing refundability of each of the new solar energy credits does not appear to achieve its intended purpose: "If a person claiming a tax credit … does not have any … tax liability, the credit may be refunded to that person." Strictly interpreted, this wording allows the credits to be refundable only in cases where a taxpayer has no tax liability. If the intention is for the credits to be generally refundable, this language should state "in the event that the available credits exceed the taxpayer's liability for the current year, the excess shall be refunded."

The bill should define "installation costs," since these serve as the basis for the new credits. Especially important is whether the eligible costs include services, tangibles or both.

OPJ/yr:njw