ECONOMIC DEVELOPMENT TAX INCENTIVE STUDY - GEOTHERMAL, SOLAR, WIND, AND BIOMASS ENERGY DEVICE TAX CREDIT

Pursuant to North Dakota Century Code Section 54-35-26, created by 2015 Senate Bill No. 2057, a variety of economic development tax incentives are to be reviewed by a Legislative Management interim committee over the ensuing six-year period. The study is aimed at ensuring that economic development tax incentives are serving their intended purposes in a cost-effective and equitable manner. This memorandum has been provided to assist in the review of the geothermal, solar, wind, and biomass energy device tax credit and provides an explanation of the incentive, the perceived goals of the Legislative Assembly in creating or altering the incentive, and the data and testimony that will be required to conduct an effective analysis of the incentive.

EXPLANATION OF THE GEOTHERMAL, SOLAR, WIND, AND BIOMASS ENERGY DEVICE CREDIT

Section 57-38-01.8 provides for a geothermal, solar, wind, or biomass energy device credit. A taxpayer may claim a credit against corporate income tax liability for the cost of a geothermal, solar, or biomass energy device installed before January 1, 2015, in a building or on a property owned or leased by the taxpayer. The amount of the credit is equal to 5 percent per year for three years of the actual cost of acquiring and installing the geothermal, solar, or biomass energy device if the device was installed before January 1, 2001, and is equal to 3 percent per year for five years if the device was installed after December 31, 2000. A taxpayer may claim a credit against individual income tax liability for the cost of a geothermal energy device installed after December 31, 2008, and before January 1, 2015, in a building or on property owned or leased by the taxpayer. The amount of the credit is equal to 3 percent per year for five years of the actual cost of acquiring and installing the geothermal energy device.

The amount of the geothermal, solar, or biomass energy device credit claimed may not exceed a taxpayer's corporate or individual income tax liability. Any credit amount exceeding a taxpayer's liability may be carried forward to each of the five succeeding taxable years for credits associated with energy devices installed through September 30, 2008, and may be carried forward to each of the 10 succeeding taxable years for credits associated with energy devices installed after September 30, 2008. For purposes of the credit, a biomass energy device is a system that uses agricultural crops, wastes, or residues; wood wastes or residues; animal wastes; landfill gas; or other biological sources to produce fuel or electricity. A geothermal energy device is a system or mechanism that provides heating, cooling, electrical, or mechanical power by extracting or converting naturally occurring subsurface energy into water or steam. A solar device is a system or mechanism that provides or stores heating, cooling, electrical, or mechanical power by converting the natural energy of the sun.

A taxpayer may claim a credit against corporate income tax liability for the cost of a wind energy device on which construction was commenced before January 1, 2015, and which is installed before January 1, 2017. The amount of the credit is equal to 5 percent per year for three years of the actual cost of acquiring and installing the wind energy device if the device was installed before January 1, 2001, and is equal to 3 percent per year for five years if the device was installed after December 31, 2000. The amount of the credit claimed may not exceed a taxpayer's corporate income tax liability. Any credit amount exceeding a taxpayer's liability may be carried forward to each of the five succeeding taxable years for credits associated with wind energy devices installed through September 30, 2008, to each of the 30 succeeding taxable years for credits associated with wind energy devices installed after September 30, 2008, and before January 1, 2012, and to each of the 10 succeeding taxable years for credits associated with wind energy devices installed after December 31, 2011. For purposes of the credit, a wind device is a system or mechanism that provides or stores heating, cooling, electrical, or mechanical power by converting the natural energy of the wind.

The first purchaser of any energy device listed in Section 57-38.5-03, and installed after December 31, 2006, is eligible to receive the credit if ownership of the energy device is transferred to the purchaser at the time installation is complete and the device is fully operational. If a taxpayer entitled to the credit is filing a consolidated return, the taxpayer may claim the credit against the aggregate North Dakota tax liability of all corporations included on the consolidated return. A passthrough entity entitled to the credit must be considered the taxpayer for purposes of the credit and the amount of credit allowed must be determined at the passthrough entity level and passed through to the corporate partners, shareholders, or members in proportion to their respective interest in the passthrough entity. Only costs directly attributable to the specified energy device may be included in determining the amount of the credit and costs for redesigning, remodeling, or altering the building in which the device is installed may not be included.
PERCEIVED GOALS OF THE LEGISLATIVE ASSEMBLY IN CREATING OR ALTERING THE GEOTHERMAL, SOLAR, WIND, AND BIOMASS ENERGY DEVICE CREDIT

Provisions regarding the geothermal, solar, wind, and biomass energy device credit were first enacted through the passage of 1977 House Bill No. 1479. As originally enacted, Section 57-38-01.8 only provided a credit for the installation costs of solar or wind energy devices. The credit could be claimed by both corporate and individual income taxpayers and was offered in an amount equal to 5 percent per year for two years of the actual cost of acquiring or installing the devices. Upon a review of the legislative history relating to the bill, the perceived goal of the Legislative Assembly in providing this exemption was to encourage investment in alternative energy sources. The estimated fiscal effect of the solar and wind energy device credit could not be determined during the 1977 legislative session.

The first modification to Section 57-38-01.8 was made during the 1981 legislative session through the passage of House Bill No. 1118. The bill served to expand the credit to pertain to costs associated with installing geothermal devices in addition to solar and wind devices. It was estimated that the provisions of House Bill No. 1118 would result in a reduction in general fund revenue in the amount of $22,000 for the 1981-83 biennium. The credit was expanded for a second time through the passage of 2001 House Bill No. 1223 which allowed the credit to be claimed by a passthrough entity and by a taxpayer installing an energy device on property leased by the taxpayer. The bill restricted the credit to costs incurred for energy devices installed before January 1, 2011, and decreased the amount of the credit for devices installed after December 31, 2000, to 3 percent of costs per year for five years. Further changes were made during the 2005 legislative session through the passage of House Bill No. 1314 which allowed a taxpayer filing a consolidated return to claim the credit against the aggregate North Dakota tax liability of all corporations included on the consolidated return and provided all qualifying taxpayers with a five-year carryforward for any earned credit amount.

Additional changes were made during the 2007 legislative session through the passage of House Bill Nos. 1514 and 1233 and Senate Bill No. 2298. Changes made during the 2007 legislative session expanded the credit to apply to the costs of installing biomass energy devices, allowed all or part of the unused credit for energy devices to be sold or transferred to the purchaser of the power generated by the device as part of the consideration in a power purchase agreement, and allowed a purchaser of an energy device installed after December 31, 2006, to be eligible for the credit if ownership of the device was transferred at the time installation was complete. Changes made during the 2009 legislative session through the passage of Senate Bill No. 2033 and House Bill No. 1277 extended the deadline from 2011 to 2015 to qualify for the income tax credit equal to 3 percent per year for five years for the actual costs of acquiring and installing the device and allowed the credit for geothermal energy devices to be claimed on the Form ND-1 income tax return.

The scope of Section 57-38-01.8 was broadened during the 2011 legislative session through the passage of House Bill No. 1124 which served to allow the credit to be claimed by individuals who install geothermal energy devices. The final modifications to credit were made during the 2015 legislative session through the passage of Senate Bill No. 2037 and House Bill No. 1228. Senate Bill No. 2037 extended the income tax credit equal to 3 percent of the installation costs each year for five years for qualifying wind energy devices. The credit, which was scheduled to expire for devices installed after December 31, 2014, was extended to include the cost of installing a wind energy device on which construction was commenced before January 1, 2015, and which is installed before January 1, 2017. House Bill No. 1228 extended the duration for which the unused portion of the credit earned for wind energy devices installed after September 30, 2008, and before January 1, 2012, could be carried forward from 20 to 30 years.

Information provided to the Political Subdivision Taxation Committee by the Tax Department on July 29, 2015, and later amended on August 12, 2015, indicates the number of individual income tax returns on which the geothermal energy device credit was claimed and the total amount claimed is as follows:

- In tax year 2009, a total of $226,501 was claimed over 147 returns;
- In tax year 2010, a total of $568,056 was claimed over 387 returns;
- In tax year 2011, a total of $876,135 was claimed over 566 returns;
- In tax year 2012, a total of $1,067,532 was claimed over 676 returns;
- In tax year 2013, a total of $1,114,837 was claimed over 693 returns; and
- In tax year 2014, a total of $1,101,791 was claimed over 625 returns.
The number of corporate income tax returns on which the geothermal, solar, wind, and biomass energy device credit was claimed and the total amount claimed is as follows:

- In tax years 2006 and 2007, the amount claimed cannot be disclosed due to confidentiality restrictions as the credit was claimed on fewer than five returns;
- In tax years 2008 and 2009, the credit was not claimed on any corporate income tax returns;
- In tax year 2010, the amount claimed cannot be disclosed due to confidentiality restrictions as the credit was claimed on fewer than five returns;
- In tax year 2011, a total of $27,705 was claimed over 5 returns; and
- In tax years 2012 through 2014, the amount claimed cannot be disclosed due to confidentiality restrictions as the credit was claimed on fewer than five returns.

DATA AND TESTIMONY REQUIRED TO CONDUCT AN EFFECTIVE ANALYSIS OF THE GEOTHERMAL, SOLAR, WIND, AND BIOMASS ENERGY DEVICE CREDIT

Data pertaining to the following items will need to be collected to effectively analyze the incentive:

1. The number of claimants;
2. The fiscal impact of the incentive;
3. Employment opportunities, business growth, or diversity in the state’s economy resulting from the availability of the incentive;
4. Negative impacts created as a result of the incentive;
5. Benefits that flow to out-of-state concerns resulting from the incentive; and
6. The use of this type of incentive in other states.

Testimony will need to be solicited from the following parties to effectively analyze the incentive:

1. The Department of Commerce;
2. The Tax Department; and
3. The North Dakota Economic Development Foundation.