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Ohio General Assembly Reforms Renewable and Advanced Energy Tax Policy

Ohio's recent Budget Bill, signed into law by Governor John Kasich, contained an important provision that significantly reduces the tax burden on certain advanced energy projects. In the last legislative session, Senate Bill 232 exempted qualifying projects from real and personal property taxation, instead requiring project owners to make payments in lieu of taxes based on generating capacity and other factors. The effect was to tax personal property used in a renewable or advanced energy project much more favorably for developers.

SB 232 was scheduled to sunset at the end of this year, but a provision in the Budget Bill extended the law. Now, a project must be under construction (or filed with the Ohio Power Siting Board) by January 1, 2014, and placed in service by January 1, 2015 to qualify for the tax treatment. The practical effect of the change is to reduce the state tax burden on renewable and advanced sources of energy generation such as solar, wind, co-generation, and clean coal, from approximately \$115,000 and \$40,000 per megawatt (MW) under the old law to a much more competitive \$6,000 to \$8,000 per MW for qualifying projects.

Highlights of Ohio's Current Law

Under the old law, any entity that generates electricity for sale to others in Ohio was deemed an "electric company" for tax purposes. Practically speaking, this means that developers of renewable and advanced energy systems who sell power to third parties (i.e., through a power purchase agreement at retail or on the wholesale market) were subject to the tangible personal property tax as a public utility. It is this utility tangible personal property tax that caused Ohio's effective tax rate on

renewable energy to be uncompetitive. Current Ohio law abates the onerous personal property tax burden on these projects and also contains a real property tax exemption, substituting a "payments in lieu of taxes" (PILOT).

- Exempt permanently from the tangible personal property tax and the real property tax any project of with a nameplate capacity¹ of 250 kilowatt (kW) or less
- Exempt "qualifying energy facilities" from real and personal property taxation upon meeting certain specified requirements that include county commissioner approval for projects of 5 MW or more
- Sunset at the end of next year (though projects placed in service by the deadline maintain the tax treatment)
- Require PILOTs of \$7,000 per MW for qualified solar projects and \$6,000 to \$8,000 per MW for all other renewable energy projects, plus clean coal and nuclear
- For all non-solar qualified energy facilities, county commissioners may negotiate additional service payments, not to exceed \$9,000 per MW when combined with the PILOT payment
- Ignore the exemption for purposes of the 3% cost cap in the state's renewable portfolio standard
- Clarify the sales and use tax treatment of related energy conversion equipment purchases
- Clarify facilities are subject to commercial activity tax but not the utility gross receipts tax.

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Public Utility Personal Property Tax Exemption

Tax Exemption for Qualified Energy Projects:

Ohio Revised Code (ORC) § 5727.75 exempts from tangible personal property tax “qualified energy projects” that meet certain criteria as certified by the director of the Ohio Department of Development (ODOD).² A qualified energy project includes any renewable energy generation as defined in the state’s renewable portfolio standard,³ as well as clean coal, advanced nuclear, and co-generation⁴. The criteria for the exemption include:

Existing Facilities: The facility did not supply electricity before December 31, 2009.

Siting/Building Permit Approval: On or before December 31, 2014, the owner⁵ must submit an application to the Power Siting Board or a political subdivision for construction. § 5727.75(B)(1)(a).

Construction Deadline: Construction must begin on or after January 1, 2009, and before January 1, 2015.⁶ § 5727.75(B)(1)(b). A construction progress report must be filed with ODOD before March 1 of each year during construction indicating percentage completed and nameplate capacity as of the previous December 31. § 5727.75(F)(2). Reports also must be filed by March 1 each year after construction indicating nameplate capacity as of the previous December 31, unless ODOD waives such requirement.

Make Annual Payment in Lieu of Taxes: Make annual service payments in lieu of taxes to the county in which the exempted property is located in the following amounts. § 5727.75(G). The PILOT is distributed in the same manner as the tangible personal property tax (to localities and school districts).

1. Solar: \$7,000 per MW.
2. Any other qualified facilities:
 - a. \$6,000 per MW if during construction the project employs 75% or more Ohio-domiciled employees.
 - b. \$7,000 per MW if during construction the project employs 60% or more Ohio-domiciled employees.
 - c. \$8,000 per MW if during construction the project employs 50% or more Ohio-domiciled employees.⁷

County Approval: For projects greater than 5 MW, the local county commissioners must approve the exemption by resolution within 30 days or else

have declared itself an “alternative energy zone.” If the county rejects the application or fails to act, the exemption is denied. County commissioners can require an additional service payment, as long as the total of the additional payment and the PILOT does not exceed \$9,000 per MW. Any additional service payment is allocated to the county general fund.

Ohio Jobs: Employment of 80% Ohio-domiciled employees⁸ in the construction of the project in the case of solar and for all other projects, more than 50%. In the case of significant wind farms, for which certification from the Power Siting Board is required under § 4906.20, the number of full-time equivalent (FTE) employees on the energy project must equal the number actually or projected to be employed in the certificate application, if such projection is required, whichever is greater. For all other energy projects, the number of FTE employees must equal the number actually or projected to be employed by ODOD, whichever is greater. § 5727.75(F)(6). ODOD will use a generally-accepted job-estimating model in use for renewable energy projects, including but not limited to the job and economic development impact model, and may adjust an estimate produced by a model to account for variables. A report on such employee numbers must be filed with ODOD. § 5727.75(F)(3).

Road Repair: For projects greater than 5 MW, repair all roads, bridges, and culverts affected by the construction to their preconstruction condition. Owner must post a bond to ensure funding for repairs.

First Responders: Provide training for fire and emergency responders for response to emergencies related to the project and, for facilities greater than 5 MW, provide any necessary equipment.

University Partnership: For projects greater than 2 MW, establish a relationship with an Ohio University or apprenticeship program for purposes of education and training. The relationship may include endowments, co-ops, internships, apprenticeships, R&D projects, and curriculum development.

RECs / Utility Right of First Refusal: Offer to sell power (or RECs) to Ohio utilities that have issued requests for proposal for such power or credits. If no request is issued on or before December 31, 2010, or no offer accepted for power or renewable energy credits within 45 days after the offer is submitted, power or credits may be sold to others.⁹

If a project meets the criteria for exemption, the exemption lasts for the life of the project if the property is placed in service before January 1, 2015 and unless ODOD revokes exemption for failure to comply with the law. § 5727.75(B)(2).

Clean Coal, Nuclear, Co-Generation: Clean coal, advanced nuclear, or cogeneration qualifies if it meets the criteria and was placed in service before January 1, 2017. § 5725.75(C)(1).

Real Property Tax Exemption: Real property included in a qualified energy project facility generally is also exempt from taxation for any tax year for which the tangible personal property that is part of the same qualified energy project is exempted (see also below). § 5725.75(D).

County Approval and Additional Service Payments: For projects greater than 5 MW in size, ODOD will forward the application for exemption to the local county commissioners and to each taxing unit in the affected counties. The county commissioners in their discretion may approve or reject the exemption. They have 30 days in which to decide. In approving an exemption, the commissioners may specify that an additional “service payment” is required. The combined total of the service payments required and the county service payment may not exceed \$9,000 per MW. § 5727.75(E)(1)(b).

Alternative Energy Zone: Rather than review each application on a case-by-case basis, the county commissioners may declare the county an “alternative energy zone” (AEZ). The resolution declaring the AEZ may specify the amount of the additional service payment required (not to exceed \$9,000 per MW).

Allocation of Service Payments: The PILOT is to be allocated just as tangible personal property tax is allocated — to local governments and school districts. Any additional service payment required by the county is to be deposited in the county general fund. § 5727.75(E)(1)(b).

RPS Cost Cap: Ohio’s renewable portfolio standard contains a “cost cap” such that utilities are not required to meet an annual benchmark to the extent compliance would raise overall generation rates by 3% or more. When calculating the cost cap, taxes are assumed to be at pre-SB 232 levels. § 4928.64(C)(3).

Reactive Power: While not necessarily tax-related, SB 232 also requires the state Public Utilities Commission to study reactive power. § 4935.10.

Post Sunset

Public Utility Tangible Personal Property Tax:

As applied to utilities generally, the tangible personal property of an electric company is assessed at one rate for generation equipment and a separate, higher rate for transmission and distribution. Questions had been raised about which portions of a wind farm or solar installation might fall into either category, (i.e., whether the wires connecting the wind turbines are “generation” or “transmission”).

Under the bill, § 5727.01 defines “energy company” as a person in the business of generating, transmitting or distributing electricity from an energy facility with an aggregate nameplate capacity greater than 250 kW. § 5727.01(D)(10). The law then subjects taxable property of an energy company to the personal property tax as a public utility. Hence, post-sunset of the bill’s exemption, systems larger than 250 kW are once again subject to the personal property tax.

An “energy facility” is one or more interconnected wind turbines, solar panels or other tangible personal property used to generate electricity from an “energy resource.” § 5727.01(P). It includes interconnection equipment, devices and related apparatus, as well as equipment that connects generators to an electricity grid or a building that consumes the electricity produced, that facilitates transmission, or that transforms voltage before delivery. It also includes buildings, structures, improvements or fixtures exclusively used to house, support or stabilize tangible personal property constituting the facility, and the land on which such property sits as is required for operation of the facility (not to exceed ½ acre for each wind turbine). “Energy resource” means any of the following: (1) “renewable energy resource” as defined in § 4928.01; (2) “clean coal technology” as described in § 4928.01(A)(34)(c); (3) “advanced nuclear technology” as described in § 4928.01(A)(34)(d); and (4) “cogeneration technology” as described (and re-defined) in § 4928.01. § 5727.01(N).

Exclusion for Certain Facilities Small Systems and Political Subdivisions:

Section 5727.02 previously had excluded certain facilities from being treated as public utilities for tax purposes. The law expands these exemptions to include a person who leases to others, or a person who owns or leases from another person, or facilities with an aggregate nameplate capacity of 250 kW or less. The new law also states a political subdivision that owns an energy facility is not supplying electricity

to others regardless of nameplate capacity if the facility's purpose is to provide electricity for the subdivision's own use.

Valuation, Assessment and Apportionment

Valuation: § 5727.11 sets forth the manner in which the true value of production and energy conversion equipment is to be determined. In both cases, the value of the property is the cost of the property as capitalized on the owner's books and records less composite annual allowances as prescribed by the tax commissioner. § 5727.11(D)(2).

Assessment: § 5727.111 sets forth the percentages of true value at which the taxable property of a public utility is assessed. The new law provides for 50% assessment in the case of a rural electric company's taxable transmission and distribution property and energy conversion equipment, and 25% for all its other property. Assessment of electric companies continues to be 85% in the case of taxable transmission and distribution property also for what the new law classifies as "energy conversion equipment."¹⁰ The valuation rate remains 24% for generation equipment. 5727.111(E)(2). In the case of an energy company, production equipment is assessed at 24% of its true value, and all other equipment is assessed at 85% of true value. § 5727.111(H).

Thus, projects built after SB 232 is scheduled to sunset will be taxed such that generation equipment (such as the wind turbines and solar panels themselves) is assessed at the rate of 24% of true value and the newly-defined "energy conversion equipment" will be assessed at the same (higher) rate as transmission and distribution equipment — 85%.

Apportionment: § 5727.15 provides for the apportionment of taxable value of public utility property to taxing districts. When all the taxable property of a public utility is located in one taxing district, the total value of the property is apportioned to that taxing district. However, when property is located in more than one taxing district, the value must be apportioned. In the case of an electric company, § 5727.15 is amended to provide that the value of energy conversion property (excluding production equipment) is apportioned to each taxing district in the proportion that the cost of such other taxable personal property located in each taxing district is of the total cost of such other taxable personal property physically located in Ohio.

For an energy company, the taxable value of all production equipment is apportioned to the tax-

ing district in which the property is located. The taxable value of all *other* property, including energy conversion equipment, is apportioned to districts in the proportion that the cost of the property located in each district bears to the total cost of all such other property.

Section 5727.06 sets forth what constitutes the taxable property of a public utility that will be assessed. As amended, the section provides that for tax years 2011 and thereafter (assuming no exemption under § 5727.75), all tangible personal property of an energy company is included if: the property was located in Ohio on December 31 of the previous year and was owned by the company or leased under a sale and leaseback transaction.

Other Taxes

Public Utility Gross Receipts Tax: § 5727.30 generally subjects public utilities to an annual gross receipts tax. However, the bill amends such section to exclude from the tax gross receipts of an electric company, rural electric company or energy company. § 5727.30(B). Thus, energy companies are exempt from the public utility gross receipts tax. They do, however, remain subject to the commercial activity tax.

Real Estate Tax: The new law exempt from real property taxation for any fixture or other real property included in an energy facility with an aggregate nameplate capacity of 250 kW or less if construction or installation is completed after January 1, 2010. § 5709.53(B).

The new law provides that the installation of an energy facility on land devoted to agricultural use will not cause the remaining portion of the tract to be regarded as a conversion of land devoted exclusively to agricultural use for "current agricultural use value" (CAUV) purposes if the remaining portion of the tract continues to be devoted to agricultural use. Nor will CAUV recoupment charges be levied for conversions incident to the construction of an energy facility. § 5713.30(B)(4).

Sales Tax: The new law clarifies that the purchase of "energy conversion equipment," defined as above in footnote 10, by a provider of electricity is exempt from sales tax. § 5739.02(B)(40). This provides energy conversion equipment the same tax-exempt treatment as other tangible personal property purchased by a provider of electricity and used for the same purposes.

Conclusion

Extension of this major reform of the state's tax code as applied to renewable and advanced energy in the Budget Bill will continue to make Ohio much more competitive with its surrounding states. Coupled with the state's strong alternative energy portfolio standard, the tax laws should help make the state a more attractive environment for investment and job creation in the advanced energy sector.

For additional information about Ohio's energy and tax law, please contact Mark Engel at mengel@bricker.com or 513.870.6565 or Maria Armstrong at marmstrong@bricker.com or 614.227.8821.

Footnotes

- 1 "Nameplate capacity" is defined as "the original interconnected maximum rated AC output of a generator or other electric production equipment under specific conditions designated by the manufacturer, expressed in the number of kilowatts or megawatts." § 5727.01(Q).
- 2 All section references herein are to the ORC.
- 3 Solar PV, solar thermal, wind, hydropower, certain solid waste, biomass, bio-methane gas, fuel cells, wind turbines on Lake Erie, off-peak storage facilities, and distributed generation utilizing renewable energy. § 4928.01(A)(35).
- 4 The definition of "co-generation" was amended to also include any electricity produced from co-generation that is sold to third parties and not simply for the primary use of the generator.
- 5 Where the statute refers to "owners" of projects, the definition generally also includes "a lessee pursuant to a sale and leaseback transaction."
- 6 Construction is deemed to begin on the earlier of the date of application for a certificate or other approval, or the date the construction contract is entered into.
- 7 Projects employing less than 50% of Ohio-domiciled employees during construction are ineligible for the tax exemption; solar projects employing less than 80% Ohio-domiciled employees during construction are ineligible.
- 8 "Full-time equivalent employee" means the total number of hours for which compensation was paid to individuals, including contract employees, employed at a qualified energy project for services performed at the project during the calendar year divided by 2,080. Owners must file a report of the total number of full-time equivalent employees and of Ohio-domiciled full-time equivalent employees employed in the construction and installation of the facility.
- 9 This "right of first refusal" does not apply if the owner or lessee: (a) is a rural electric company or municipal power agency; (b) is a person who, before completion of the project, contracted for the sale of power or credits with a rural electric company or municipal power agency; or (c) contracts for the sale of power or credits from the project before the effective date of the legislation.
- 10 "Energy conversion equipment" as defined in § 5727.01 is all tangible personal property connected to a wind turbine tower, connected to and behind solar radiation collector areas and designed to convert the radiant energy of the sun into electricity or heat, or connected to any other property used to generate electricity from an energy resource, through which electricity is transferred to controls, transformers or power electronics and to the transmission interconnection point. Such equipment also includes inverters, batteries, switch gears, wiring, collection lines, substations, ancillary tangible personal property, or any lines and associated tangible personal property located between substations and the transmission interconnection point. § 5727.01(N).

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