The Business, Entrepreneurship & Tax Law Review

Volume 1
Issue 1 *Spring 2017*

Article 10

2017

Clean Energy Tax Credits: Creating an Energy Welfare State or Saving the Planet

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CLEAN ENERGY TAX CREDITS: CREATING AN ENERGY WELFARE STATE OR SAVING THE PLANET?

K. Alex Langley*

I. INTRODUCTION

"We've subsidized oil companies for a century. That's long enough. It's time to end the taxpayer giveaways to an industry that rarely has been more profitable and double down on a clean energy industry that never has been more promising. Pass clean energy tax credits."[1] In his 2012 State of the Union Address, President Barack Obama made expanding clean energy one of his priorities for his second term in office. Energy has always been a public policy concern; however, when gas prices reach unreasonable levels, politicians and voters raise an outcry for clean energy and relief from foreign oil.[2] Yet, when gas prices drop,

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1 Barack Obama, President of the U.S., 2012 State of the Union Address (Jan. 24, 2012) (transcript available at https://www.whitehouse.gov/the-press-office/2012/01/24/remarks-president-state-union-address).

2 Senator Bill Nelson, *Breaking the Foreign-Oil Habit*, POLITICO (Apr. 15, 2012, 9:45 PM), http://www.politico.com/story/2012/04/energy-independence-is-possible-and-

Americans are all too willing to forget about reducing the country's dependence on oil and looking for sustainable renewable energy sources. Instead of cycling through this mentality for decades, Americans need to take the opportunity presented now to end the cycle.

As early as the 1970s, Congress recognized a need to move away from oil and gas as the country's only sources of energy.[3] Congress adopted a tax incentive program to promote the development of existing clean energy resources as well as to encourage the development of technology that would increase the efficiency of clean energy.[4] However, history has demonstrated that these tax credit incentives were not enough. While clean energy technology has become more reliable and more readily accessible, clean energy production is still far more expensive than fossil fuel production.[5]

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necessary-075151.

[3] Molly F. Sherlock, *Energy Tax Policy: Historical Perspectives on Current Status of Energy Tax Expenditures*, CONGRESSIONAL SERVICE REPORT, 1 (May 2, 2011), http://www.leahy.senate.gov/imo/media/doc/R41227EnergyLegReport.pdf.

[4] *Id.* at 2.

[5] *Tax Subsidies*, INSTITUTE FOR ENERGY RESEARCH, http://data.instituteforenergyresearch.org/energy-subsidies-vs-btu-output/ (last visited June 19, 2017). Additionally, clean energy receives a "tax preference subsidy per unit of production" of $0.83. *Id.*

This article addresses possible tax incentives that may be available in addition to or as an alternative to current tax credits. First, it will provide an overview of America's ever-evolving energy policy. This section explains why the country's energy policies resemble a rollercoaster. Second, this article offers a brief history of tax credits, specifically clean energy tax credits and fossil fuel tax credits. Part three describes Master Limited Partnerships ("MLPs") and Real Estate Investment Trusts ("REITs"), two tax-flavored entity choices used by the oil and gas industry to improve their bottom line. Specifically, part three explores the tax benefits of forming an entity under this model as opposed to a corporation or partnership.

Part four discusses criticisms waged against clean energy tax credits including why many conservatives oppose these tax credits yet support fossil fuel tax credits. Finally, the article proposes that clean energy entities should be allowed to reorganize as REITs or MLPs. In addition, Congress should extend clean energy tax credits for another five years, with phase-outs. This article concludes that combining new tax structures for clean energy with guaranteed tax credits for five years will bring stability to the energy markets and move the country one step closer to its lofty goal of ending its dependence on foreign oil, and providing a stable source of clean energy for generations to come.

II. CLEAN ENERGY TAX CREDITS

Energy has always been a hot-button topic, not only in the environmental field, but also in the tax field. Congress has been concerned about the ever-demanding energy needs in the United States, but has tried various policies in an attempt to keep energy prices low.[6] Policies have been in one of two camps. When global crises have threatened crude oil production or when oil-per-barrel prices were skyrocketing, Congress placed more tax incentives into alternative energy. However, when oil-per-barrel prices were extremely low and crude was freely flowing, Congress was less inclined to give tax breaks for renewable energy.[7]

A. *Historical Perspective*

America's tax policy regarding energy credits can be divided into five time frames.[8] The first era, from the early 1900s to the 1970s, saw the promotion of oil and gas. In 1916, Congress introduced a provision that

[6] Salvatore Lazzari, *Energy Tax Policy: History and Current Issues*, CONGRESSIONAL SERVICE REPORT, 1 (June 10, 2008), https://www.fas.org/sgp/crs/misc/RL33578.pdf.
[7] *Id.*
[8] Sherlock, *supra* note 3, at 2.

allowed gas and oil companies to deduct fully the cost of intangible drilling instead of having those costs amortized over time. Later, in 1926, Congress created a provision that allowed companies to deduct a "fixed percentage of gross receipts rather than a deduction based on the actual value of the resources extracted."[9] These oil-and gas-friendly policies continued to characterize America's tax policy up until the 1970s.[10]

In the 1970s, the United States was reeling from both foreign and domestic issues including an increase in governmental spending without a comparable raise in the national gross product ratio, which led to a sharp budget deficit.[11] Additionally, the country faced an energy crisis as a result of the Arab Oil Embargo.[12] Many Americans who drove cars during the early 1970s still remember waiting in lines at gas stations for hours, only to learn that the stations had run out of gas before they reached the front of the line. Moreover, the Iranian Revolution in 1979 led to a dramatic

[9] *Id.* at 3.
[10] *Id.* While tax policies changed during the 1970s these two particular policies live on today in a more limited form. *Id.*
[11] Noureil Roubini & Jeffrey Sachs, *Government Spending and Budget Deficits in the Industrial Economies* (Nat'l Bureau of Econ. Research, Working Paper No. 2919, 1989), http://www.nber.org/papers/w2919.
[12] Sherlock, *supra* note 3, at 3.

increase in the cost of oil.[13] Additionally, during this decade, the country became focused on preserving the environment. During the 1970s the Environmental Protection Agency ("EPA"), Earth Day, the Natural Resources Defense Council ("NRDC"), the National Oceanographic and Atmospheric Administration ("NOAA"), and the Clean Water Act ("CWA") were all created in response to the sudden awareness of our place in the universe.[14] People also had a growing concern over the use of nuclear energy after the Three Mile Island disaster.[15]

As a result, Congress increased taxes on oil and gas, decreased these companies' tax deductions, and started providing cleaner energy tax incentives.[16] For example, Congress first created new taxes for oil companies including the "'gas guzzler' tax,[17] a windfall profit tax on oil,[18]

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[13] *Id.*
[14] *Environmental Movement Timelines*, PBS, http://www.pbs.org/pov/ifatreefalls/environmental-timelines/ (last visited June 19, 2017).
[15] *Id.*
[16] Sherlock, *supra* note 3, at 4.
[17] This tax was enacted to dissuade individuals from purchasing fuel-inefficient cars. Interestingly, this tax did not apply to SUVs, trucks, or minivans because they were uncommon. The tax applied to passenger cars only. *Gas Guzzler Tax*, EPA, https://www.epa.gov/fueleconomy/gas-guzzler-tax (last updated Feb. 14, 2017).
[18] This tax was enacted to decrease oil company profits so they could be redistributed to the taxpayers. However, the tax, and generally these types of taxes, does not increase the United States' revenue significantly. Salvatore Lazzari, *The Crude Oil Windfall Tax of the 1980s: Implications for Current Energy Policy*, CONGRESSIONAL SERVICE REPORT, (Mar. 9, 2006),

and an excise tax on petroleum (the "[s]uperfund" program)."[19] Additionally, Congress enacted new tax incentives for cleaner, unconventional fuels; many of these subsidies were part of the Energy Tax Act[20] of 1978.[21]

In the 1980s, many of these tax policies were renewed; however there was a subtle shift in policy as a result of the election of President Reagan.[22] The Reagan presidency was marked by an opposition to tax credits for energy companies across the board.[23] Many of the tax subsidies enacted under the Energy Tax Act were allowed to expire.[24] Additionally, because the price of oil continued to decline, many of the oil tax credits that were enacted in the early 1970s were allowed to expire; however, two of the primary tax credits from the early 1900s continued.[25]

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http://www.taxhistory.org/thp/readings.nsf/cf7c9c870b600b9585256df80075b9dd/b9e4d38fed6cbf7f8525745900099a55?OpenDocument.

[19] Sherlock, *supra* note 3, at 3.

[20] Energy Tax Act of 1978, Pub. L. No. 95-618, 95 Stat. 3174. The Act also included tax credits for homeowners who made their homes greener through the instillation of energy efficient products. It also included a tax credit for business that invested in clean energy. Sherlock, *supra* note 3, at 4.

[21] Sherlock, *supra* note 3, at 4.

[22] *Id.* at 5.

[23] *Id.*

[24] *Id.* at 4.

[25] *Id.* at 5. Specifically, the deductibility of intangible drilling costs and the percentage depletion tax credit were allowed to continue. *Id.*

The Reagan era tax policies did not last long, and soon Congress enacted new tax credits, which were influenced by low crude oil prices.[26] The Omnibus Budget Reconciliation Act of 1990[27] created a tax of $0.5 per gallon of gas and created a tax credit for the recovery of oil expenditures.[28] Additionally, the Energy Policy Act of 1992[29] was passed under President Bush, which included a number of tax credits for clean energy.[30] First, Congress enacted a credit for the creation of wind power or biomass-created electricity.[31] The provisions were later extended under the Tax Relief Extension Act,[32] which also expanded oil and gas tax credits.[33] Later, President Clinton's Congress "proposed a differential British thermal unity (BTU) tax on fossil fuels, which was ultimately dropped in favor of an excise tax increase on motor fuels."[34]

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[26] *Id.*
[27] Omnibus Budget Reconciliation Act of 1990, Pub. L. No. 101-508, 104 Stat. 1388.
[28] Sherlock, *supra* note 3, at 5. The Act also "expanded the unconventional fuel product credit and introduced a tax credit for small ethanol producers. Additionally the act "reduced the effect of the alternative minimum tax on oil and gas investments." *Id.*
[29] Energy Policy Act of 1992, Pub. L. No. 102-468, 106 Stat. 2776.
[30] Sherlock, *supra* note 3, at 5.
[31] *Id.* at 5-6. The Act also included tax deductions for clean energy vehicles, tax credits for alcohol based fuels, and credits for unconventional fuels. Additionally, tax credits were introduced for oil and gas entities. *Id.* at 6.
[32] Tax Relief Extension Act of 1999, Pub. L. No.106-170, 113 Stat. 1860.
[33] Sherlock, *supra* note 3, at 6.
[34] *Id.* Additionally, the Omnibus Budget Reconciliation Act of 1993, which contained a per gallon tax on oil. *Id.*

The early 2000s were marked by rising oil prices and calls for comprehensive energy legislation.[35] More recently, Congress has leaned toward a tax policy encouraging individuals and businesses to be more environmentally friendly in their day-to-day practices. For example, individuals can seek tax credits for a number of purchases, including energy-efficient appliances.[36] While few complain about paying lower taxes, many have voiced concern over the disproportionate dollar amount of tax breaks that Congress has given to clean energy companies when compared to fossil fuel companies; especially with the fall of crude oil prices to the lowest in recent memory.

B. *Current Clean Energy Tax Credits*

Currently, there are a number of tax credits available for businesses in the energy industry. One credit is the New Clean Renewable Energy Bond, which more than doubled the maximum amount of funds available for companies to issue clean energy bonds.[37] Additionally, the Internal Revenue Service ("IRS") has continued to extend the "eligibility

[35] *Id.*
[36] *Federal Income Tax Credits for Efficienc*y, ENERGY STAR, https://www.energystar.gov/about/federal_tax_credits (last visited June 19, 2017).
[37] *Energy Incentives for Business in the American Recovery and Reinvestment Act*, IRS, https://www.irs.gov/uac/Energy-Incentives-for-Businesses-in-the-American-Recovery-and-Reinvestment-Act (last updated Mar. 6, 2017).

dates" for many of the tax credits, allowing businesses to continue limiting their tax liability.[38]

Another important tax credit is the Investment Tax Credit ("ITC").[39] In 2005, Congress passed the ITC, which established a 30% tax credit for commercial fuel cell property, solar energy production, and some wind energy production.[40] Later in 2008, the tax credit was extended through the Emergency Economic Stabilization Act of 2008.[41] The Act also allowed entities that paid the alternative minimum tax to receive the credit.[42] While the Obama Administration was attempting to phase out all of these tax credits, it has thus far been unsuccessful. In effect, these tax credits "distort[] markets by encouraging more investment in the oil and natural gas industry."[43]

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[38] *Id.*
[39] *Solar Investment Tax Credit (ICT)*, SOLAR ENERGY INDUSTRIES ASSOCIATION, http://www.seia.org/policy/finance-tax/solar-investment-tax-credit (last visited June 19, 2017).
[40] *Id.*
[41] Energy Economic Stabilization Act of 2008, Pub. L. No. 110-343, 122 Stat. 3765.
[42] *Solar Investment Tax Credit (ICT*), *supra* note 39.
[43] *End Existing Subsidies*, POLICY SOLUTIONS, https://www.energypolicy.solutions/docs/end-existing-subsidies.html (last visited June 19, 2017).

C. *Fossil Fuel Tax Benefits*

Currently, fossil fuel companies are afforded a number of federal tax subsidies. First, they are allowed to deduct "intangible drilling costs" ("IDC") up to "30[%] of the IDCs on productive wells [, these] must be capitalized and amortized over a 60-month period."[44] Annually, this subsidy costs the federal government $1.495 million.[45]

Another subsidy is a provision that allows domestic oil and natural gas producers to amortize their "geological and geophysical expenditures" over two or seven years.[46] It is estimated that this costs the federal government $305 million annually.[47] Coal, lignite, and shale companies can also take advantage of a deduction for the companies' depletion of hard mineral fossil fuels.[48]

While not a current tax credit, at one point, the costs of oil and natural gas wells that produced less than 25 barrels per day could be

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44 Treasury Dep't, *United States—Progress Report On Fossil Fuels Subsidies*, TREASURY.GOV, 2, https://www.treasury.gov/open/Documents/USA%20FFSR%20progress%20report%20to%20G20%202014%20Final.pdf (last visited June 19, 2017).
45 *Id.*
46 *Id.* at 4.
47 *Id.*
48 *Id.*

currently deducted rather than being amortized over time.[49] However, because oil and gas prices were so high, the federal government cut the tax benefit.[50] It is possible that this tax benefit could return because the price of oil has dramatically declined.[51] Also, it is interesting to note that unlike Clean Energy subsidies, many of the tax provisions regarding fossil fuels do not have an expiration date.

III. ALTERNATIVE TAX STRUCTURES

While tax credits have been useful in keeping clean energy a viable option, in addition to coal and crude oil, these tax credits cannot be sustained indefinitely. Additionally, clean energy companies need predictability in tax law. In order for these companies to create one year, five year, and ten year business plans, they need to know in year one whether in year two there will be a tax credit allowing them to save $2 million in taxes, as these tax savings can be put back into the business to

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[49] *Id.* at 6.
[50] *Id.*
[51] *Id.* "Reduction as oil and gas prices increase (A) In general The $3 and 50 cents amounts under paragraph (1) shall each be reduced (but not below zero) by an amount which bears the same ratio to such amount (determined without regard to this paragraph) as—(i) the excess (if any) of the applicable reference price over $15 ($1.67 for qualified natural gas production), bears to (ii) $3 ($0.33 for qualified natural gas production)." The applicable reference price for a taxable year is the reference price of the calendar year preceding the calendar year in which the taxable year begins. 26 U.S.C. § 451 (2012).

expand it. Currently, benefits that are available in one year are allowed to expire the next year, only to be renewed retroactively in the third year. This hurts clean energy businesses' efforts to survive in the market, let alone excel.

Because of the uncertainties of tax credits, other tax benefits must be explored. One such benefit is an expansion of business entities available to the industry. In order for clean energy, such as wind, hydroelectricity, and solar energy, to become truly competitive with fossil fuels, clean energy corporations need to be structured as entities similar to those in the oil and gas industry, in order to reap the same tax benefits that keeps fossil fuel companies profitable. This includes allowing clean energy corporations to be structured as Master Limited Partnerships ("MLPs") and Real Estate Investment Trusts ("REITs"). Each structure will be explored below.

A. *Master Limited Partnerships*

A Master Limited Partnership[52] ("MLP") is a publicly traded entity whose interest is traded on national exchanges such as NASDAQ.[53]

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[52] 26 U.S.C. § 7704 (2012).

"(a) General Rule For purposes of this title, except as provided in subsection (c), Typically, these entities are created as Delaware limited partnerships.[54] Alternatively, an MLP could be organized as a Delaware limited liability company.[55]

MLPs have been in existence since the 1980s.[56] Apache Oil ("Apache") was the first company to use the MLP structure in 1981.[57] Apache was able to leverage the unique structure of the MLP to gather

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> a publicly traded partnership shall be treated as a corporation (b) Publicly Traded Partnership For purposes of this section, the term 'publicly traded partnership' means any partnership if—(1) interest in such partnership are traded on an established securities market, or (2) interests in such partnership are readily tradable on a secondary market….(c) Exceptions for Partnerships with Passive-Type Income….(2) Gross Income Requirements A partnership meets the gross income requirements of this paragraph for any taxable year if 90[%] or more of the gross income of such partnership for such taxable year consists of qualifying income….(d) Qualifying Income For purposes of this section—(1) In General Except as otherwise provided in this subsection, the term 'qualifying income' means—(A) interest, (B) dividends, (C) real property rents, (D) gains for the sale or disposition of real property (including property described in section 1221(a)(1)), (E) income and gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resources (including fertilizer, geothermal energy, and timber), industrial source carbon dioxide, or the transportation or storage of any fuel described in subsection (b), (c), (d), or (e) of section 6426 [alcohol based fuels, biodiesel mixtures, and alternative fuels]…"

Id.

[53] Latham & Watkins LLP, *Master Limited Partnerships*—101, LP, https://www.lw.com/MLP-Portal/101 (last visited June 19, 2017).

[54] *Id.*

[55] *Id.*

[56] *Id.*

[57] Legg Mason, *Master Limited Partnerships: An Introduction*, FINANCE INSTITUTE, 3 (Sept. 2013), http://www.finance-inst.co.il/image/users/171540/ftp/my_files/xx/D13408-mpls-an-introduction-MIPX015929.pdf?id=13496849.

numerous small investors because Apache was able to offer "[investors] a partnership investment in an affordable and liquid security."[58] Other companies watched Apache benefit from gathering numerous small investors to grow a company instead of looking for a few large investors.[59] Soon many oil and gas companies started restructuring as MLPs.[60] Restructuring led to an extraordinary growth in entities forming as MLPs, which alarmed Congress.[61]

Congress was afraid that too many entities would form as MLPs and would therefore destroy the large amount of income tax derived from corporations which are subject to double taxation.[62] Therefore, Congress severely limited the use of MLPs in the late 1980s by restricting the types of entities that could be structured as a MLP, but allowed traditional energy entities to remain organized as MLPs.[63] "Congress responded by revamping the tax code, creating strict parameters for business to follow in

[58] *Id.*
[59] *Id.*
[60] *Id.*
[61] Latham & Watkins, LLP, *supra* note 53.
[62] Legg Mason, *supra* note 57 at 3. Corporations are taxed twice, whereas partnerships will be taxed only once. This dramatically decreases the amount of money an entity will pay in taxes, therefore decreases how much money the government is taking in. Beth Laurence, *How Corporations Are Taxed*, NOLO, http://www.nolo.com/legal-encyclopedia/how-corporations-are-taxed-30157.html (last visited June 19, 2017).
[63] Latham & Watkins, LLP, *supra* note 53.

order to benefit from the MLP structure. The new rules narrowed the scope to a select range of natural resource activities that qualified for MLP status."[64] Today, there are hundreds of MLPs, and the majority of them are in the business of storage and transportation of energy.[65] MLPs naturally offer the best tax planning opportunities for new clean energy enterprises, especially given the need for renewable energy, the constant improvement in technology, and the ever-increasing need to store energy.[66] Because they are taxed as partnerships, they are subject to only one level of tax and have flexibility in allocating profits and losses to their members, while at the same time providing free transferability of interests similar to corporations.

There are a number of requirements needed to qualify as an MLP. First, an MLP must receive most of its income as "qualifying income," only 10% of an MLP's income can come from non-qualifying sources.[67] If this requirement is not met, the entity will lose all of it's tax advantages

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[64] Legg Mason, *supra* note 57 at 3.
[65] *Id.* at 4.
[66] *Id.* at 2.
[67] Latham & Watkins, LLP, *supra* note 53.

and will be treated as an ordinary corporation.[68] "Qualifying income includes…. income and gains derived from exploration, development, mining or production, processing, refining, transportation…or the marketing of any mineral or natural resource as well as certain passive-type income including interest, dividends and real property rents."[69] However, Congress has commented on the definition of qualifying income, specifically targeting renewable items.[70] In 1988, Congress decided that renewable items such as water, air, and corn, were not qualifying income for MLPs.[71]

However, in 2008 the definition of qualifying income was amended again to include the storage of "alternative fuels such as biodiesel and ethanol."[72] Congress defined qualifying income to hinder clean energy further by allowing only income generated by moving oil and gas through pipelines.[73] Specifically, moving oil by "truck, rail or barge to a retail outlet" does not meet the definition of qualifying income.[74] Most

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68 *Id.*
69 *Id.*
70 *Id.*
71 *Id.*
72 *Id.*
73 *Id.*
74 *Id.*

green energy cannot be transported by pipeline and can only be transported by other means, such as by trucks or rail, which are specifically excluded by Congress.

If an entity can meet all of these requirements, then it can reap the benefits of an MLP. The biggest tax benefit MLPs receive is the ability to have only one level of taxation.[75] Typically, MLPs are not taxed like a corporation.[76] When corporations make distributions there are two levels of taxation.[77] First, the shareholder is taxed on the distribution; commonly taking the form of a dividend.[78] Second, the corporation is taxed on the distribution as income.[79] Partnerships, on the other hand, are taxed only once.[80] These entities are considered pass through entities.[81] This allows the partnership to pass along all of its income and assets on to the shareholders and partners.[82] This also allows a partnership to pass along its tax liability onto the shareholders and partners.[83] While green energy

[75] Legg Mason, *supra* note 57, at 2.
[76] *Id.*
[77] *Id.*
[78] *Id.*
[79] *Id.*
[80] *Id.*
[81] Latham & Watkins, LLP, *supra* note 53.
[82] *Id.*
[83] *Id.*

companies are taxed twice, fossil fuel companies are only taxed once, because Congress specifically prohibited green energy companies from receiving this tax benefit.[84]

B. *Real Estate Investment Trusts*

A Real Estate Investment Trust[85] ("REIT") is an entity that owns real estate that produces income.[86] REITs were created in 1960 under the Cigar Excise Tax Extension.[87] Organizing an entity as a REIT allows "investors the opportunity to invest in large-scale, diversified portfolios of income-producing real estate."[88] In 1965, Continental Mortgage Investors was one of the first REITs to come into existence and be listed on the New

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[84] *Id.*

[85] A real estate investment trust is defined as "A corporation that is given special income tax treatment in order to allow individuals to invest in real estate through centralized management without being subject to corporate income taxes. REITs fall into two basic categories: companies that invest directly in real estate so as to have equity ownership of it; and companies that lend funds and take mortgages on real estate. The income of a REIT is not taxed to the corporation but rather is taxed directly to the shareholders. In order to qualify as a REIT, a corporation must: (1) be organized in the United States; (2) have at least 100 shareholders; (3) have a high percentage of its assets invested in real estate and its income derived from real estate; and (4) meet other technical requirements." *Real Estate Investment Trust*, BARRON'S LAW DICTIONARY (6th ed. 2010).

[86] NAREIT's Home For All Things REIT, *What is a REIT?*, REIT, https://www.reit.com/investing/reit-basics/what-reit (last visited June 19, 2017).

[87] NAREIT's Home For All Things REIT, *REIT Industry Timeline*, REIT, https://www.reit.com/investing/reit-basics/reit-industry-timeline#0 (last visited June 19, 2017).

[88] NAREIT's Home For All Things REIT, *supra* note 86.

York Stock Exchange.[89] The first major change for REITs occurred in 1974 when Congress passed property foreclosure rules.[90] The Act allowed REITs to operate previously foreclosed property for a short period of time and then turn the property over to an independent contractor.[91] REITs also changed under the Tax Reform Act of 1976 when Congress allowed "REITs to be established as corporations in addition to business trusts."[92]

REIT's requirements differ in some respects from MLP's requirements. First, REITs are only required to have 75% of their income derived from qualifying sources. To be qualified income, the income must come from property, either through mortgages or from the sale of property.[93] Additionally, 75% of the entities' assets must be real estate.[94] Similar to MLPs, REITs must "[p]ay at least 90[%] of its taxable income in the form of shareholder dividends each year."[95] There are additional requirements for REITs including a minimum number or shareholders, a certain managerial structure, organized as a corporation, and "no more

[89] NAREIT's Home For All Things REIT, *supra* note 87.
[90] *Id.*
[91] *Id.*
[92] *Id.*
[93] NAREIT's Home For All Things REIT, *supra* note 86.
[94] *Id.*
[95] *Id.*

than 50% of its shares held by five or fewer individuals."[96] REITs are similar to corporations. They are publicly traded entities, are sold on major stock exchanges, and are accessible to the average investor.[97] This allows individuals to buy stock in a REIT and then receive dividends, depending how well the entity did that year.[98] It also allows individuals to diversify their investment portfolios without having to purchase real estate directly.

While fossil fuel companies can take advantage of favorable tax structures, such as MLPs and REITs, currently, companies in the clean energy field, including solar and wind farms, cannot. The next section of this article calls for Congress to expand the definition of qualifying income to include renewable energies, including the transportation of the energy. This will start to level the playing field between fossil fuel entities and clean energy companies.

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[96] *Id.*
[97] *Id.*
[98] *Id.* Similar to MLP's, REITs are traded on public stock exchanges, but unlike MLPs there are public REITs, private REITs, and non-public REITs. These REITs can be traded on public stock exchanges. These types of REITs must also be registered with the Securities and Exchange Commission ("SEC"). *Id; see also* NAREIT's Home For All Things REIT, *Frequently Asked Questions About REITs,* REIT, https://www.reit.com/investing/reit-basics/frequently-asked-questions-about-reits (last visited June 19, 2017).

IV. Proposal To Encourage Renewable Energy

This article proposes that the definition of qualified income under § 7704(d))(1)(E) should be expanded to include the exploration, development, production, processing, refining, transportation, marketing, and storage of any renewable energy, including but not limited to solar-derived energy, wind-derived energy, hydro-derived energy, and bioenergy. This proposed definition would allow clean energy companies to reorganize as REITs and MLPs because it would allow the income derived from the sale of clean energy to be included under qualified income. Additionally, allowing clean energy companies to restructure as REITs and MLPs would allow them to take advantage of only one level of taxation, as opposed to the two levels of taxation they currently face because they are structured as corporations.

This proposition is not radical. Similar propositions have come before Congress. In 2015, Congressmen Coons, Moran, Poe, and Thompson introduced the Master Limited Partnerships Parity Act ("Bill").[99] The Bill would amend the Internal Revenue Code "to extend the

[99] Ernst & Young, *Master Limited Partnership Alert: Reintroduced Bill Would Make MLP Structure Available to Certain Renewable Energy Activities*, EY (July 2015),

publicly traded partnership ownership structure to energy power generation projects and transportation fuels, and for other purposes."[100] Specifically, the Bill would create a new subsection for the qualified income definitional section by incorporating the definition of resources under 26 U.S.C. § 45 of the Internal Revenue Code.[101] Additionally, it would add ten new subsections to the definition section of 26 U.S.C. § 7704, including: "electricity storage devices—The receipt and sale of electric power that has been stored in a device directly connected to the grid" and "renewable chemicals—The production, storage or transportation of any qualifying renewable chemical."[102] While the Bill is currently waiting to be voted upon in the Senate, the substance of the Bill would allow currently clean energy companies to reorganize as MLPs. Additionally, the Bill has many improvements from previous attempts to

http://www.ey.com/Publication/vwLUAssets/EY-reintroduced-bill-would-make-mlp-structure-available-to-certain-renewable-energy-activities/$FILE/EY-reintroduced-bill-would-make-mlp-structure-available-to-certain-renewable-energy-activities.pdf.

[100] H.R. Res. 2883, 114th Cong. (2015).

[101] *Id.*; *see also* 26 U.S.C. § 45(c)(1)(A)-(I) "wind, closed-loop biomass, open-looped biomass, geothermal energy, solar energy, small irrigation power, municipal solid waste, qualified hydropower production, and marine hydrokinetic renewable energy."

[102] H.R. Res. 2883, 114th Cong. (2015).

include clean energy as a qualified income for MLPs. Previous versions only expanded the definition to include solar energy derived income.[103]

However, issues arise when the Bill purports to not only expand a definition, which is difficult in and of itself, but also adds numerous sections that are only going to inflame oil and gas lobbyists more. Additionally, the Bill would only address MLPs and not REITs. While the Bill expands the definition to include all clean energy companies, some of these entities might function better as a REIT instead of a MLP. For example, solar farms would benefit from organizing as REIT, as opposed to a MLP, because solar farms require dealing with real estate. Additionally, there has already been a push to allow solar farms to operate as REITs.[104] Allowing solar farms to be organized as REITs would allow smaller investors to interact with the clean energy market without the fears associated with fossil fuels because once the farm is "running, it produces electricity without risk of the price of its fuel increases…with very low risk of plant failure (and if it does fail, its likely only offline for a short

[103] Ernst and Young, *surpa* note 99.
[104] Tom Konrad, *Solar REITs: A Better Way to Invest in Solar*, GENESIS NANOTECH (Oct. 22, 2012), https://genesisnanotech.wordpress.com/tag/master-limited-partnership/.

time, no risk of explosion), and relatively low overhead in terms of maintenance."[105]

Additionally, there are benefits in lobbying for the definition of qualified income for REITs over MLPs because changing the definition of MLPs require an act of Congress, whereas the REIT definition can be changed through an IRS revenue ruling.[106] In fact, The Renewable Energy Trust Capital, Inc., has already made a request to the IRS for such a revenue ruling.[107] This would, overnight, allow solar energy companies to reorganize as REITs but would leave other clean energy companies in the dust. Additionally, the REIT structure lends itself to wind farms, as well.[108]

This could especially effect Missouri because it has limited oil resources but has numerous opportunities for wind and solar farms. Missouri is fortunate to have "large tracts of windy land and fertile soil, located relatively close to dense, energy-consuming urban centers, [which] put [Missouri] in a prime position to become a national leader in

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105 *Id.*
106 *Id.*
107 *Id.*
108 *Id.*

renewable energy."[109] Missouri is a wind haven and its estimated that the state can "keep its energy dollars at home and even start exporting energy to other states."[110] The state legislature has made a commitment that solar power will account for 2% of the state's energy consumption.[111] Additionally, solar farms are popping up all over the state, including: Kansas City, St. Louis, Columbia, and Springfield.[112] In fact, Missouri is ranked tenth in the nation for in its use of solar power.[113]

In addition to passing the Bill to allow clean energy entities to operate as MLPs and an IRS revenue ruling expanding the definition to REITs to include wind and solar farms, Congress still needs to do more. In order to ensure stability for clean energy companies, Congress needs to commit to a clean energy tax credit plan for at least five years. The paper proposes that all of the current clean energy tax credits remain, but be phased out over the five-year period. Moreover, fossil fuel tax credits

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[109] *Economic Opportunities of Cutting Carbon Pollution and Climate Change in Missouri*, NAT. RESOURCES DEF. COUNCIL (Mar. 2014), https://www.nrdc.org/sites/default/files/carbon-pollution-state-jobs-MO.pdf.
[110] *Id.*
[111] *Id.*
[112] Associated Press, *2 Missouri Cities Consider Solar Energy Farms*, WASHINGTON TIMES (Jan. 5, 2015), http://www.washingtontimes.com/news/2015/jan/5/2-missouri-cities-consider-solar-energy-farms/.
[113] *Id.*

should be phased out over a three-year period or simply ended immediately. This would give clean energy companies time to reorganize and tax plan accordingly for five years. With this stability, investors can have faith that the markets will allow clean energy MLPs and REITs the time necessary to attract investors by offering them limited time tax credit opportunities. This will invigorate the market and bring a new level of competition to the energy marketplace.

A. *The Critics*

While many environmentalists cringe at the idea of cutting clean energy tax credits, a substantial portion of the political population vehemently opposes any clean energy tax credits. "Manipulating the tax code to prop up an industry where growth is entirely dependent on a tax credit does not make a 'highly successful policy.'"[114] Many in this political camp argue that green energy tax credits only manipulate the system and keep alive energy alternatives that are not sustainable.

For example, The Heritage Foundation ("Heritage"), a conservative thinktank, argues that these tax breaks create a clean energy

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[114] Mallory Carr, *Absent Tax Credits, The Free Market Works for Wind Energy*, THE DAILY SIGNAL (Feb. 7, 2014) http://dailysignal.com/2014/02/07/absent-tax-credits-free-market-works-wind-energy/.

welfare state.[115] Heritage argues that these credits "misallocate labor and capital by shifting resources away from more competitive use[s]."[116] They allege that these tax credits allow solar energy producers to out-bid each other by bidding negative numbers because the "producers will collect the $22 per megawatt hour generated from the tax credit."[117] Heritage's answer to America's energy crisis is to "end the current inefficient system of picking winners and losers in the energy sector" by ending tax credits.[118]

Heritage is not alone. Warren Buffet has spoken out about the perceived failure of clean energy in the past and argues that its continued support through tax credits is irresponsible.[119] Because man cannot control how many windy or sunny days there will be, clean energy facilities are extremely inefficient and cannot survive without backup energy

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[115] Nicolas Loris, *EFEPA Eliminates Corporate Welfare and Corporate Dependence,* THE HERITAGE FOUND. (Jan. 15, 2013), http://www.heritage.org/research/reports/2013/01/energy-tax-credits-impact-of-energy-freedom-and-economic-prosperity#_ftn1.
[116] *Id.*
[117] *Id.*
[118] *Id.*
[119] Nancy Pfotenhauer, *Bing Wind's Bogus Subsidies*, U.S. NEWS & WORLD REP. (May 12, 2014, 2:30 PM), http://www.usnews.com/opinion/blogs/nancy-pfotenhauer/2014/05/12/even-warren-buffet-admits-wind-energy-is-a-bad-investment.

resources.[120] U.S. News argues that "when lawmakers give special tax breaks to their friends and favorite industries, they shift the burden onto everybody left in the tax base. While subsidies may allow wind turbine makers to pump up their payrolls, the rest of the economy suffers as a result."[121]

Other grassroots movements have gone so far as to argue that these tax breaks need to end immediately because of the amount of damage they have caused. Americans for Prosperity has repeatedly lobbied for ending clean energy tax credits because "taxpayers have sadly seen little return for their forced investment in wind energy over the past decade," and these credits are only a handout for energy companies, wasting millions of taxpayers' hard earned dollars.[122]

All of these organizations push the idea that the free market should control what kind of energy should be available to consumers, which is a logical argument because America has a strong laissez faire bent and its markets operate on a supply and demand cycle. For example, coal

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[120] *Id.*
[121] *Id.*
[122] Brent Wm. Gardner, *AFP Supports PTC Elimination Act*, AMERICANS FOR PROSPERITY (Apr. 22, 2015), https://americansforprosperity.org/afp-supports-ptc-elimination-act/.

companies are allowed to treat royalties as capital gains.[123] Additionally, coal companies receive tax credits for investing in cleaner mining techniques and are allowed to exclude benefits for disabled miners.[124] Further, in 2005, under the Energy Policy Act, non-green energy companies could receive a 20% tax credit for creating "clean coal facilities."[125] While oil and coal energy receives the least amount of tax credits as compared to other energy sectors, in 2012, the coal and oil sector received an average of 520 million in tax credits.[126]

B. *Responding to the Critics*

Some of these accusations are not as far fetched as one might expect. It really is impossible to know if the tax credits are merely propping up a failed market and turning it into an energy welfare state. However, how can the market decide when clean energy companies are not being given the same basic tax advantages as fossil fuel entities simply because solar farms cannot organize as REITs? Furthermore, it is impossible for green energy companies to compete when investors are

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[123] INSTITUTE FOR ENERGY RESEARCH, *supra* note 5.
[124] *Id.*
[125] *Id.*
[126] *Id.*

constantly fearful of losing tax credits and the companies themselves cannot adequately tax plan. Also, clean energy companies should be allowed the same tax benefits that fossil fuel companies have been given for years, like favorable amortization and accelerated deductions. Once fossil fuel entities and clean energy companies are treated equally the free market can decide if both or only one is truly sustainable.

Instead of repeating history and merely enjoying the low prices at the gas pump, this is the time to change America's tax policies toward clean energy by changing the structure of clean energy companies. This will allow clean energy companies to take advantage of tax credits currently allowed and compound the savings by reducing their tax liability by reorganizing their companies.

This will allow clean energy companies a better chance to be on equal footing as oil and coal companies.[127] With the price of producing clean energy dropping steadily,[128] the tax code should be rewritten in order

[127] Because oil and coal companies have been in business longer, these industries are considered to be the backbone on Americas labor force, and the sheer amount of money these groups have for lobbying it will take clean energy companies longer to be equal to fossil fuel companies. However, allowing these companies to structure themselves like non-clean energy companies will at least allow them to gain a foothold in America's energy fabric.

[128] Adnan Z. Amin, *The Falling Costs of Renewable Energy: No More Excuses*,

to allow clean energy companies the ability to form MLPs and REILs in order to lower their tax liabilities, therefore reducing the need for federal tax credits.

V. Conclusion

73%, that is how many people in the United States prefer alternative energy, such as wind and solar energy, to oil and gas.[129] Hitting a record high of supporters, compared with a Gallup poll conducted on the topic back in 2012, where only 59% of the country supported such an expansion.[130] This fact, combined with polls recording the highest percentages of Americans concerned with global warming.[131]

While most Americans agree that having sustainable energy is a concern, parties differ on how to address the issue. At this point in time, it is simply impossible to know which camp is correct. Could wind farms become sustainable without government intervention? If clean energy cannot be sustained with government handouts, then are we not creating

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HUFFINGTON POST (Nov. 26, 2015), http://www.huffingtonpost.com/adnan-z-amin/post_10557_b_8600240.html.

[129] Zac Auter, *In U.S. 73% Now Prioritize Alternative Energy Over Oil, Gas*, GALLUP (Mar. 24, 2016) http://www.gallup.com/poll/190268/prioritize-alternative-energy-oil-gas.aspx?g_source=CATEGORY_ENVIRONMENT_AND_ENERGY&g_medium=topic&g_campaign=tiles.

[130] *Id.*

[131] *Id.*

another energy welfare state?[132] But, how can we really know if this is the case, if the coal and oil industries are any different since they also receive tax credits? Also, it is unfair to say that clean energy is unsustainable if it is being cut off at the knees because of the inability to form as REITs or MLPs? For these reasons Congress should not renew tax credits for the fossil fuel industry to continue. Congress should immediately allow clean energy entities to restructure themselves as a REIT or MLP and should renew clean energy tax credits for a five-year period with a gradual phase out over that five year period. This will allow clean energy companies to compete on equal footing with fossil fuel companies. In the wise words of Adam Smith, the invisible hand of the markets should decide the fate of clean energy.

[132] Loris, *supra* note 115.