July 17, 2017

The Honorable Orrin Hatch  
U.S. Senate Committee on Finance  
219 Dirksen Senate Office Building  
Washington, D.C. 20510

Re: Removing Impediments and Disincentives for Energy Efficiency Investments in the Current Tax System

Dear Chairman Hatch:

Thank you for the opportunity to provide comments on the potential for tax policy to incentivize investment in energy efficiency.

Advancing energy efficiency presents an enormous untapped opportunity to tackle our toughest energy and environment challenges while at the same time unleashing American economic activity and productivity. It is an indispensable, undervalued solution that, when strategically promoted in the tax code, can create jobs, enhance energy security, and lower harmful emissions and improve U.S. competitiveness in global markets—all while stabilizing peak demands on our overstressed grid.

Unfortunately, as of January 1, 2017, the U.S. tax code includes no meaningful provisions that incentivize energy efficiency. We strongly recommend the Committee address this in its ongoing deliberations on tax reform and are pleased to provide several proposals for how this could be done.

Energy efficiency gains made since 1973 have cut energy waste dramatically to fuel the U.S. economy more productively, saving Americans almost $1 trillion every year in avoided energy costs. Energy efficiency is also a leading job-creator in the energy sector. Currently, 2.2 million workers across construction, manufacturing, wholesale trade, and professional and business service industries are employed, in whole or in part, in the energy efficiency sector. Incentivizing investments in energy efficiency through the tax code will only continue to drive job creation and economic growth for families and businesses across the U.S.

The opportunity before Congress to enact meaningful tax reform should include a portfolio of incentives and policies that both increase capital investment in energy efficiency and reduce the upfront cost of purchasing energy-efficient equipment. By improving the environment for capital investments and addressing the commercial costs of efficiency improvements simultaneously, tax reform could drive down energy consumption and increase savings for homeowners, consumers, businesses, hospitals and institutions of higher education, and state local governments.
Tax policies suited to energy efficiency should generally leverage the inherent cost-effectiveness of measures, match the life-cycle and duration of time when savings and other benefits accrue, and lower up-front costs that are too frequently a deterrent to investment. Furthermore, Congress should approach tax policy in a way that promotes the use of public-private partnerships (P3s), performance contracting, and residential and commercial building energy efficiency. Thoughtful tax policy—aimed at areas of specific need and customized to the individual, corporate, or governmental entity—should simultaneously enable and direct investments toward energy efficiency.

Energy efficiency has long enjoyed the support of both Republicans and Democrats. In 2005, Congress passed on a bipartisan basis legislation that included targeted tax incentives that stimulated energy-efficient investments in new and existing homes and commercial buildings. These incentives expired on December 31, 2016. Reinstating these incentives should be among the first actions taken to encourage investments in energy efficiency. Additionally, we respectfully recommend:

- Providing accelerated depreciation for energy-efficient equipment and building components, with shorter depreciation periods for more efficient purchases;
- Expanding the use of master limited partnerships (MLPs) for energy efficiency projects;
- Ensuring the long-term availability of tax-exempt status for municipal bonds used for efficiency improvements;
- Expanding the use of private activity bonds (PABs) for state and local government buildings; and
- Exempting water utility rebates from federal income taxes.

Additional information on these recommendations can be found in the enclosed attachment. Thank you for your consideration. The Alliance and our membership stands ready to support your efforts by providing any additional information you require. Please feel free to contact Alliance Vice President for Policy and Research Daniel Bresette at (202) 857-0666 with questions or to request additional information.

Sincerely,

Kateri Callahan
President

Encl.
Re: Removing Impediments and Disincentives for Energy Efficiency Investments in the Current Tax System

1. Tax Credits and Deductions

On December 31, 2016, three energy efficiency tax incentives, which have helped homeowners and businesses save money and cut energy use by investing in energy-efficient homes and equipment, expired after Congress failed to extend them before the end of the 114th Congress. In the residential sector, the Section 25C Nonbusiness Energy Property Credit for Existing Homes and the Section 45L Energy Efficient Home Credit have been particularly effective in reducing energy bills. Sec. 25C provides a 10 percent tax credit for the purchase of certain nonbusiness energy-efficient measures up to $500, providing an incentive for homeowners to invest in efficiency improvements and choose energy-efficient products over less-efficient alternatives. Sec. 45L provides builders up to $2,000 for homes that use 50 percent less energy (compared to the 2006 International Energy Conservation Code) for heating and cooling and a $1,000 tax credit for new manufactured homes that achieve 30 percent energy savings for heating and cooling or ENERGY STAR requirements. Since the 45L credit was enacted in 2005, the number of homes that qualify by using 30-50 percent less energy for heating and cooling has jumped from less than 1 percent to about 11 percent.

In the commercial sector, the Sec. 179D Commercial Building Tax Deduction promotes energy efficiency in commercial and multifamily buildings, which account for more than 20 percent of energy consumption in the United States. This incentive provides above-the-line deductions of up to $1.80 per square foot for energy efficiency improvements to lighting, heating, cooling, ventilation, hot water systems, and the building envelope. According to an American Institute of Architects study, renewing the tax deduction would create as many as 77,000 new design and construction jobs annually over two years along with almost $7.4 billion more in annual GDP. “The economic growth and job creation generated by a modernized Section 179D would result in a striking GDP return of ten to one when considering the cost of the tax policy,” the study finds.

2. Accelerated Depreciation

The current depreciation periods for many types of equipment are significantly longer than their average service lives. HVAC systems, lighting installations, and roofing are depreciated over 39 years under current law; however, these components typically last for only 15 to 25 years. When the equipment inevitably fails before the end of the depreciation period, many businesses opt to repair the equipment rather than replace it with an updated, more efficient product to avoid taking a financial hit by writing off the undepreciated value. Considering the efficiency developments that occur over 40 years, businesses could save a significant amount of money and energy if there was not a disincentive to replace equipment when its service life has expired.
By refining cost recovery periods to match the service life of equipment, manufacturers would also be incentivized to increase efficiency in their products thereby making U.S. manufacturers more competitive with their counterparts abroad. As more efficient products decrease the amount of energy used per dollar of economic output, manufacturers and businesses work together to drive both economic productivity and environmental stewardship.

Additionally, full expensing at time of investment is another solution that has been proposed, including by members of the House of Representatives leadership and the Trump campaign last year, to address this disincentive and stimulate investment.

3. **Master Limited Partnerships Parity Act**

The Master Limited Partnership (MLP) market exceeds $400 billion in low-cost capital investments for fossil energy that have not been available for clean energy. According to a National Renewable Energy Laboratory (NREL) study, financing charges can raise the overall cost of clean energy by up to 50 percent.

To address this issue, Sens. Chris Coons (D-Del.), Jerry Moran (R-Kan.), and Reps. Ted Poe (R-Texas) and Mike Thompson (D-Calif.), introduced the Master Limited Partnerships Parity Act (S.1656 and H.R. 2883) in the 114th Congress to help level the playing field by allowing energy generation and renewable fuel companies form MLPs. The MLP Parity Act makes power generation from renewables, renewable fuels and related energy activities eligible to form MLPs, including energy efficiency projects in buildings, electricity storage, and combined heat and power. The subsection of the bill that deals with energy-efficient buildings applies to companies that develop projects in commercial and large multifamily buildings. Expanding that to include all buildings would provide the same advantages to companies that develop and execute performance contracts in federal and MUSH (municipal, university, school, and hospital) markets. According to a Brookings analysis, the Joint Committee on Taxation’s (JCT’s) scoring suggests that clean energy MLPs could raise $18 billion in the first five years with a market capitalization of $60 billion after a decade. With a projected cost of $993 million to the taxpayer, a $60 billion return presents an excellent return.

4. **Tax-Exempt Bonds**

Allowing local and state government entities in the MUSH sector to issue tax-exempt bonds for Energy Savings Performance Contracts—like they can for other infrastructure projects—creates another avenue for financing energy efficiency projects across an enormous sector of the economy. The MUSH sector could issue tax-exempt bonds to raise capital for ESPC projects and repay the bond holders through the resulting savings. For example, private activity bonds (PABs) are issued to finance various types of facilities owned or used by private entities, including airports, docks and certain other transportation-related facilities; water, sewer and certain other local utility facilities; solid and hazardous waste disposal facilities; certain residential rental projects (including multi-family housing revenue bonds); and certain other types of facilities. Currently, government buildings are missing from this list. If included, PABs could be used to finance ESPC projects in the MUSH sector.
H.R. 960, introduced by Rep. Mike Kelly (R-Pa.) during the 115th Congress, would amend the Internal Revenue Code to provide for tax-exempt financing of certain government-owned buildings by expanding the definition of “exempt facility bond” to include bonds used for qualified government buildings, including: schools, universities, libraries, courts, hospitals, public safety facilities, or government offices. In this case, MUSH sectors in states with enabling legislation would be able to use PABs to raise the capital needed to finance the upfront cost of energy efficiency projects.

5. Water Utility Rebates

Rebates from energy utilities are tax-exempt, but not rebates from water utilities. This means that water utilities must provide 1099s to customers that have received $500 or more in water rebates at the end of the year. This serves as a disincentive to water efficiency retrofit programs and other efforts. An expansion of the tax-exempt status of rebates from electric and natural gas utilities to include rebates from water utilities would contribute to lower upfront costs for water efficiency improvements to customers and save energy and reduce wasted water consumption. A bipartisan proposal that would provide this exemption, H.R. 448, the Water Conservation Rebate Tax Parity Act, was introduced in January. Efficiency measures that provide customers new ways to better control their water usage have positive upstream benefits of lower overall stress on strained distribution systems.