

Financing Our Energy Future Act

A bill to level the playing field by giving investors in renewable energy projects access to a decades-old corporate structure with a tax advantage now available only to investors in fossil fuel-based energy projects

U.S. SENATOR CHRIS COONS

At a time when the United States needs to increase domestic energy production and leaders of both political parties say they support an “all of the above” energy strategy, Congress should level the playing field and give all sources of domestic energy — renewable and non-renewable alike — a fair shot at success in the marketplace.

The federal government should not be in the business of picking winners and losers in the energy market, but for nearly 30 years, that’s exactly what it has been doing with a provision in the tax code that authorizes the formation of master limited partnerships (MLPs). An MLP is a business structure that is taxed as a partnership, but whose ownership interests are traded on a market like corporate stock.

By statute, MLPs have only been available to investors in energy portfolios for oil, natural gas, coal extraction, and pipeline projects. These projects get access to capital at a lower cost and are more liquid than traditional financing approaches to energy projects, making them highly effective at attracting private investment. Investors in renewable energy projects, however, have been explicitly prevented from forming MLPs, starving a growing portion of America’s domestic energy sector of the capital it needs to build and grow.

The *Financing Our Energy Future Act* is a straightforward, powerful tweak to the federal tax code that could unleash significant private capital into the energy market.

The legislation would level the playing field between traditional and new energy businesses by helping energy-generation and transmission companies form master limited partnerships, which combine the funding advantages of corporations and the tax advantages of partnerships.

By allowing additional forms of energy development to access this market tool, we can go beyond political rhetoric and start delivering an all-of-the-above energy strategy.

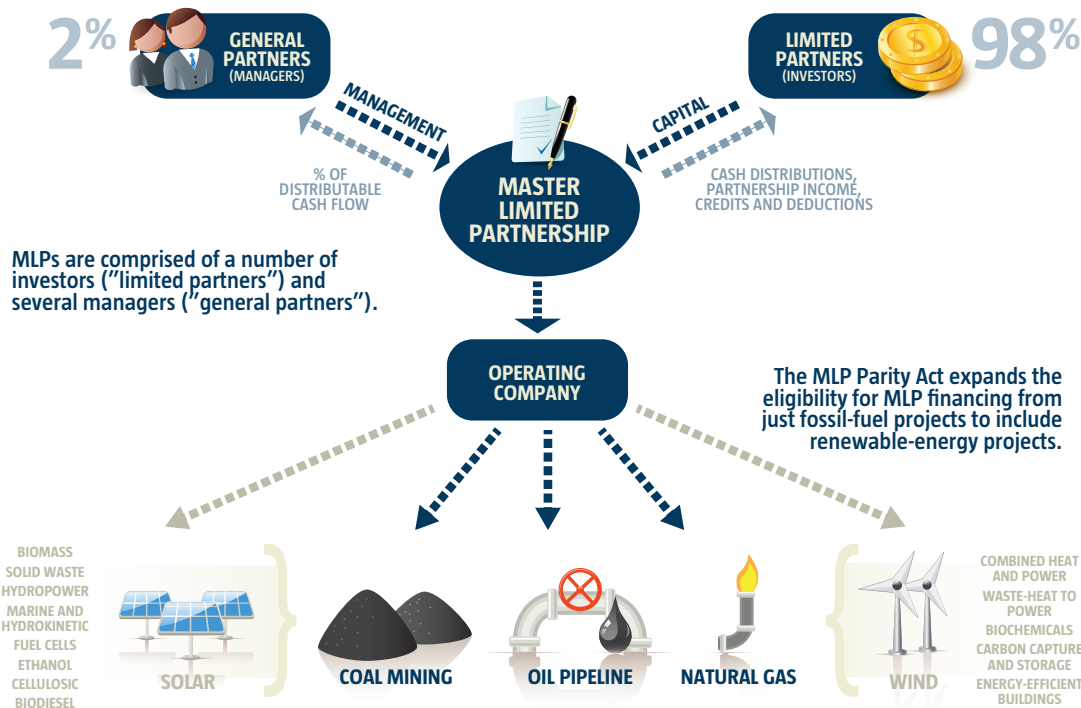
MLPs combine the funding flexibility of a corporation with the tax benefits of a partnership, creatively stimulating private investment in energy projects.



HOW MASTER LIMITED PARTNERSHIPS WORK

An MLP is a business structure that is taxed as a partnership, but whose ownership interests are traded on a market like corporate stock. Whereas profit from publicly traded C corporations is taxed at both the corporate level and the shareholder level, income from MLPs is taxed only at the shareholder level because it is treated as a partnership for tax purposes.

An MLP consists of limited partners (investors) and general partners (managers). The limited partners — who can number in the thousands — provide capital and receive quarterly required distributions generally equivalent to shareholder dividends in a C-corporation. They play no role in the operation of the MLP, while the general partners manage the MLP's daily operations. General partners can take the form of another company or a group of individuals, typically holding a 2 percent ownership stake.



Writing in the *New York Times* in June 2012, Dan Reicher and Felix Mormann of Stanford University's Steyer-Taylor Center for Energy Policy and Finance described the appeal of MLPs: "Master limited partnerships carry the fund-raising advantages of a corporation: ownership interests are publicly traded and offer investors the liquidity, limited liability and dividends of classic corporations. Their market capitalization exceeds \$350 billion. With average dividends of just 6 percent, these investment vehicles could substantially reduce the cost of financing renewables."

Because MLPs are so attractive to investors, they have been proven to bring new capital into American energy projects. This is especially important in the case of renewable-energy generation, where it is harder for investors to see as quick a return as compared to fossil fuel-based energy generation, for which much of the processing and transportation infrastructure was built decades ago. Constructing the same level of critical infrastructure for renewable energy sources will take time and investment, so the *Financing Our Energy Future Act* levels the playing field and helps address that problem.

An MLP must generate at least 90 percent of its income from qualified sources, such as real estate or natural resources, including crude oil, natural gas, petroleum products, coal, timber, and other minerals. Section 613 of the federal tax code specifically requires qualifying energy

The Financing Our Energy Future Act has been endorsed by:

American Council for an Energy-Efficient Economy (ACEEE)
 American Council on Renewable Energy (ACORE)
 Advanced Biofuels Business Council
 Algae Biomass Organization
 Alliance for Industrial Efficiency
 Alliance to Save Energy
 Amazon
 Biotechnology Innovation Organization (BIO)
 BPC Action
 Carbon180
 Carbon Capture Coalition
 Center for Climate and Energy Solutions (C2ES)
 Ceres
 Clean Air Task Force
 Covanta Energy
 Energy Storage Association
 Fuel Cell and Hydrogen Energy Association
 Growth Energy
 International District Energy Association
 Master Limited Partnership Association
 National Association of State Energy Officials (NASEO)
 National Hydropower Association
 Natural Resources Defense Council (NRDC)
 National Wildlife Federation
 Solar Energy Industries Association (SEIA)
 Third Way



What are the benefits of an MLP?

Pass-through tax structure (no double taxation) leaves more cash to distribute to investors

Cash distributions are mostly tax-deferrable

Lower cost of capital provides MLPs with advantages in building and acquiring assets

Public trading allows MLPs to raise capital from a broader range of investors than if not traded

Can own rate-regulated assets and still give investors an attractive rate of return

Greater management control than in corporations. Some corporations drop assets into an MLP so the market can realize their value while the corporate parent still controls them.

From the National Association of Publicly Traded Partnerships

sources to be depletable resources – meaning we are working against our own goal of an “all of the above” energy strategy that includes additional homegrown renewable energy sources.

How the Financing Our Energy Future Act Helps

The bill simply expands the definition of “qualified” sources to include clean energy resources and infrastructure projects. Specifically included are those energy technologies that qualify under Sections 45 and 48 of the tax code, including wind, closed and open loop biomass, geothermal, solar, municipal solid waste, hydropower, marine and hydrokinetic, fuel cells, and combined heat and power.

The legislation also allows for a range of transportation fuels to qualify, including cellulosic, ethanol, biodiesel, and algae-based fuels, as well as energy-efficient buildings, electricity storage, carbon capture and storage, renewable chemicals, and waste-heat-to-power technologies.

The *Financing Our Energy Future Act* does not affect any current MLP entity. All projects currently eligible to structure as MLPs would continue to qualify exactly as they would under existing law.

**MIKE McADAMS, PRESIDENT,
ADVANCED BIOFUELS ASSOCIATION**

“Substantial investments by private companies in research and development have been the catalyst for today’s success in bringing advanced biofuels to commercial markets, but stable and consistent public policies are crucial to encourage and allow additional investment dollars that will help get us across the finish line.”

HISTORY OF MASTER LIMITED PARTNERSHIPS

The first MLP was created in 1981 to attract capital by offering small investors a partnership investment in a liquid security. The success of the Apache Oil Company MLP led to other oil and gas MLPs, as well as MLPs formed for other capital-dependent enterprises.

Congress first established rules for master limited partnerships in 1987 legislation that introduced Internal Revenue Code Section 7704 and, for the first time, defined “publicly traded partnerships.” The MLP structure was limited to businesses deriving 90 percent of their income from specific sources, including dividends, rents, interests, capital gains, and mining and natural resources income identified in Section 613 of the tax code. This definition allowed oil and gas extraction and transportation activities access to the MLP structure, but excluded other energy sources.

In 2008, the *Emergency Economic Stabilization Act* (P.L. 110-343) expanded the definition of qualifying income to include transportation and storage of certain renewable and alternative fuels (ethanol, biodiesel, and a series of liquefied fuels), as well as industrial-source carbon dioxide.

The National Association of Publicly Traded Partnerships estimates there are more than 100 MLPs currently being traded on major exchanges, primarily focused on energy-related industries and natural resources. “Midstream” oil and gas projects – gathering, processing, pipelines, and distribution – account for the majority of current MLPs.

Of the estimated \$445 billion in MLP capital currently in the market, approximately \$400 billion (89 percent) has gone into qualifying energy and natural resources. Of that, just under 80 percent has gone into midstream oil and gas pipeline projects.

	MLP	LLC	Corporation
Taxable at entry level	No	No	Yes
Tax items flow through	Yes	Yes	No
Tax deferral on distributions	Yes	Yes	No
Tax reporting	K-1	K-1	DIV-1099
General partner	Yes	No	No
IDRs	Yes	No	No
Investor voting rights	No	Yes	Yes

Source: National Association of Publicly Traded Partnerships



Broad Support for FOEFA

Lori Ziebart, Executive Director, Master Limited Partnership Association: “In 1987, Congress passed legislation that established the modern day MLP, with the intent to promote domestic investment in the extensive buildout of our nation’s energy infrastructure. Over more than three decades, the industry has been tremendously successful and effective in raising hundreds of billions of dollars of capital through this highly efficient market-based structure. The MLP model remains a critical way the industry raises capital today to support the significant and ongoing buildout of this essential U.S. energy infrastructure network. This ultimately results in lower cost and more reliable energy for consumers. With the introduction of the Financing Our Energy Future Act, we commend Senators Coons and Moran for their commitment to the MLP structure and recognition of the valuable role it can play in the development and advancement of additional energy resources and related infrastructure.”

David Terry, Executive Director, National Association of State Energy Officials (NASEO): “The National Association of State Energy Officials supports a balanced national energy policy. The Financing Our Energy Future Act, if enacted, would be a critical element of such policy balance. We strongly encourage its adoption.”

Mark P. Allen, President and Chairman, Algae Biomass Organization: “The Financing Our Energy Future Act will open up the master limited partnership tax-advantaged corporate structure to investors ready to finance the growth of renewable energy, carbon capture and utilization, and other vital low carbon products being deployed by the algae industry. The members of the Algae Biomass Organization thank Senators Coons and Moran, and Representatives Estes and Thompson for their leadership in introducing the Act in the 116th Congress. Allowing MLPs to bring new capital to industry innovation and growth will help create jobs and enhance our energy and environmental security. Algae-based clean technology companies look forward to competing on the level playing field this bill will help ensure.”

Noah Deich, Executive Director, Carbon180: “Carbon180 commends Senators Coons and Moran and Representatives Estes and Thompson for introducing the Financing Our Energy Future Act, which will support the commercialization of clean energy technologies including carbon capture, use, and storage here in the US. This bill recognizes that captured carbon dioxide can be utilized economically in many different applications – such as concrete, plastics, graphite, carbon fiber, fuels and chemicals – and it creates financial incentives that can help drive innovation in these technologies in a way that protects industrial jobs, tackles climate change today, and paves the way for carbon dioxide removal solutions in the future.”

David Gardiner, Executive Director, Alliance for Industrial Efficiency: “We applaud Senators Coons (D-DE) and Moran (R-KS) for their bipartisan leadership in introducing the Financing Our Energy Future Act. For the past century, conventional fuels have been able to access low-cost financing to support infrastructure development. This bill levels the playing field for renewables and clean-energy technologies, encouraging investment into the energy infrastructure of tomorrow. The Alliance for Industrial Efficiency is particularly pleased that the bill extends low-cost financing to Combined Heat and Power (CHP) and Waste Heat to Power (WHP), proven clean-energy sources that could provide as much as 20 percent of U.S. electric capacity. Despite this tremendous potential, these technologies currently represent only 8 percent of U.S. electricity. The Financing Our Energy Future Act will lower the cost of financing such projects, sending a strong signal about the value of such investments. By lowering financial hurdles to CHP and WHP, this bill helps put these technologies on an equal footing with conventional fuels. The sponsors of this bill are right to recognize that U.S. investments in renewable and clean-energy technology can save substantial amounts of energy and money, make American manufacturing more competitive globally, and help create jobs in our country.”

Kurt Waltzer, Managing Director, Clean Air Task Force: “The Financing Our Energy Future Act will provide an important financial pathway for commercializing cleaner advanced technologies. Carbon capture, for example, is a critical-path technology for decarbonizing our energy production. Allowing these projects access to MLPs will help accelerate its deployment and cost reduction, and ultimately its wide-scale commercial use.”

Stephanie Batchelor, Acting Executive Vice President, Industrial & Environmental Section, BIO: “Countless companies are working to secure a sustainable American energy future and reduce our reliance on foreign oil, and it’s important they have the necessary tools to be successful. Unfortunately, today, an antiquated tax provision is preventing environmentally friendly technologies from accessing capital and slowing the transformation to a 21st-century, bio-based economy that will produce clean, affordable energy and create high-quality jobs. With the Financing Our Energy Future Act, we can better finance and foster innovative renewable chemicals and biofuels to combat climate change, provide Americans with low carbon energy, and revitalize domestic manufacturing. BIO thanks Senators Coons and Moran and Representatives Thompson and Estes for recognizing the need to level the playing field and embrace new energy opportunities.”



Jason Hartke, President, Alliance to Save Energy: “If we intend to meet our climate goals, we need to find ways to mobilize investments in energy efficiency and other technologies at a greater scale than ever before. The bipartisan, bicameral Financing Our Energy Future Act represents a new opportunity to deliver the benefits of energy efficiency—job creation, energy cost savings, and lower carbon emissions—by leveraging a tax structure currently reserved for fossil-fuel energy projects. I urge Congress to pass this bill and encourage the use of master limited partnerships for energy efficiency as quickly this session as possible.”

Gregory Wetstone, President and CEO, American Council on Renewable Energy (ACORE): “We welcome the introduction of the Financing Our Energy Future Act, which would help level the playing field in capital markets by making master limited partnerships available to renewable energy technologies. The ongoing transition to America’s renewable energy economy will require meaningfully greater levels of capital investment, and we thank Senator Coons, Senator Moran, Congressman Thompson and Congressman Estes for their leadership in bringing forward this common-sense, bipartisan legislation.”

Paula Soos, Vice President Government Affairs, Covanta Energy: “This important bipartisan legislation will help create a more robust domestic energy market, importantly allowing a broad range of renewable technologies equal access to important capital financing structures. Covanta applauds Senators Coons and Moran for their leadership on policy which positively impacts renewable energy generation like waste-to-energy, and helps state and local governments achieve resiliency and climate change goals.”

Dan Reicher, Founding Executive Director, Steyer-Taylor Center for Energy Policy and Finance and Lecturer, Stanford University: “Expanding access to MLP financing will do much to address U.S. economic, environmental and security imperatives by lowering the cost and accelerating the deployment of a range of clean energy technologies. The bill comes at an opportune moment as renewable energy tax credits begin to phase down. MLP-supported investment could provide a long-term source of cost-effective finance to renewables, just as it has for U.S. oil and gas pipelines for decades. The Financing Our Energy Future Act would also provide important financial support to carbon capture, utilization, and storage as that technology proves itself from an engineering perspective but still has challenges economically. Finally, MLPs could help advance various types of electricity storage technologies critical to large-scale deployment of a number of renewable energy sources.”

Kelly Speakes-Backman, CEO, Energy Storage Association: “ESA supports the efforts of Senators Coons & Moran and Representatives Thompson & Estes to introduce the bipartisan Financing Our Energy Future Act. Including energy storage as an eligible asset for master limited partnerships would allow energy infrastructure providers to build and acquire energy storage technologies at lower cost, accelerating the transition to a more resilient, efficient, sustainable and affordable energy infrastructure. Coupled with the Energy Storage Tax Incentive and Deployment Act (S. 1142 / H.R. 2096), which ESA also endorses, the Financing our Energy Future Act will help establish a long-term tax framework to accelerate storage deployment.”

Bob Perciasepe, President, Center for Climate and Energy Solutions: “Natural resource developers have long benefited from a variety of tax incentives. The time is ripe to make carbon capture and renewable projects eligible for Master Limited Partnership (MLP) financing, which can provide favorable tax treatment for investors. Together with the 45Q carbon storage tax credit, the MLP tool will improve the private financing capacity of carbon capture projects with little cost to the taxpayers. Thanks to Sens. Coons and Moran, and Reps. Thompson and Estes, for their bipartisan, bicameral effort. It is time for Congress to pass the Financing Our Energy Future Act.”

Abigail Ross Hopper, President and CEO, Solar Energy Industries Association: “Today, solar is a bright spot in our nation’s economy, employing 242,000 workers at more than 10,000 U.S. companies. We need strong tax policies to support renewable energy. The MLP proposal has the potential to attract private sector investment for critically-important solar projects.”

Brad Crabtree, Co-Director, Carbon Capture Coalition: “The Carbon Capture Coalition is pleased to support the bipartisan Financing Our Energy Future Act. We applaud the sponsors Senators Chris Coons (D-DE) and Jerry Moran (R-KS) and Representatives Mike Thompson (D-CA) and Ron Estes (R-KS) for recognizing the importance of carbon capture as a key element of our nation’s broader portfolio of energy technologies. This legislation will ensure the availability of tax-advantaged master limited partnerships (MLPs) as a tool for financing carbon capture and utilization projects, thereby reducing the cost of equity and providing project developers with access to capital on more favorable terms. Making carbon capture and utilization projects eligible for the MLP structure is recommended in the Coalition’s recently-released consensus federal policy blueprint as part of a suite of policies needed to build on the 45Q tax credit to foster economywide deployment of carbon capture, which will support American energy production and create highly-skilled, good-paying jobs, all while reducing carbon emissions.”



OP-ED

How to Make Renewable Energy Competitive

By **FELIX MORMANN** and **DAN REICHER**June 1, 2012 | <http://nyti.ms/LmGDI7>*The New York Times*

STANFORD, Calif. — Renewable energy needs help. Technological innovation has significantly reduced the cost of solar panels, wind turbines and other equipment, but renewable energy still needs serious subsidies to compete with conventional energy. Today, help comes mostly in the form of federal tax breaks.

These tax incentives, and the Congressional battle over extending them for wind projects beyond the end of this year, mean that other, more powerful policies to promote renewables are not getting the attention they deserve. If renewable energy is going to become fully competitive and a significant source of energy in the United States, then further technological innovation must be accompanied by financial innovation so that clean energy sources gain access to the same low-cost capital that traditional energy sources like coal and natural gas enjoy.

Two financial mechanisms that have driven investment in traditional energy projects — real estate investment trusts and master limited partnerships — could, with some help from Washington, be extended to renewable energy projects to lower their cost and make America's energy future cleaner, cheaper — and more democratic.

Federal support for renewable energy today consists primarily of two tax breaks: tax credits and accelerated depreciation rates. But both tools have a very limited reach. Only investors with hefty tax bills, typically big banks or corporations, can exploit them to reduce their tax burden. Most potential investors, including tax-exempt pension funds and, importantly, retail investors trading stocks, don't have big enough tax bills to exploit the break. As a result, the few remaining players whose considerable tax bills place them in the market for tax breaks are able to demand returns of up to 30 percent for investing in renewable energy projects — an investment known as “tax equity.”

There are better options. They may sound wonky, but they could prove revolutionary.

Real estate investment trusts, or REITs, which are traded publicly like stocks, could tap far broader pools

of capital to vastly lower the cost of financing renewable energy. REITs have a market capitalization of over \$440 billion while paying shareholders average dividends below 10 percent — roughly a third of the cost of tax equity investments for renewable energy.

Master limited partnerships carry the fund-raising advantages of a corporation: ownership interests are publicly traded and offer investors the liquidity, limited liability and dividends of classic corporations. Their market capitalization exceeds \$350 billion. With average dividends of just 6 percent, these investment vehicles could substantially reduce the cost of financing renewables.

But current law makes using both of these investment vehicles for renewable energy difficult if not impossible. Washington could help in two ways. First, the Internal Revenue Service needs to clarify the eligibility of renewable power generation for REIT financing. Second, Congress needs to fix a bizarre distinction in the tax code that bars master limited partnerships from investing in “inexhaustible” natural resources like the sun and wind, while allowing investments in exhaustible resources like coal and natural gas. In 2008, as surging gasoline prices were infuriating American voters, Congress amended the tax code to enable master limited partnerships to invest in alternative transportation fuels like ethanol. We should treat power sources, like wind and solar farms, similarly.

There is hope. Senator Chris Coons, Democrat of Delaware, plans to introduce a bill to allow master limited partnership investment in renewable energy. This approach is preferable to a recent proposal by Senator Bernard Sanders, independent of Vermont, and Representative Keith Ellison, Democrat of Minnesota, to eliminate this investment option for fossil-fuel projects. Both moves would level the playing field between conventional and renewable energy, but the Coons bill does so by promoting, rather than limiting, economic growth across the energy industry.

These approaches could help renewable energy projects reduce their financing costs up to fivefold. These cost

improvements could significantly reduce the price of renewable electricity and, over time, erase the need for costlier subsidies. Of course, making renewable energy eligible for master limited partnership and REIT financing would amount to a new kind of subsidy, because both are exempt from income tax. Indeed, some members of Congress fear that expanding master limited partnerships will erode the federal tax base. We don't think so. Investors in master limited partnerships and REITs still pay taxes on dividends. Moreover, these investments would most likely bring many more renewable energy projects online, actually raising overall tax revenue.

A more valid concern is whether renewable energy master limited partnerships might be abused as tax shelters, reminiscent of what happened in the 1980s California “wind rush.” Back then investors cared more about putting turbines in the ground to secure tax credits to lower their tax bill on other income than whether the machines actually produced electricity.

History, however, need not repeat itself. Renewable energy master limited partnerships can guard against such abuse by ensuring that these tax privileges actually result in green electricity.

There's another benefit to expanding the pool of renewable energy investors: It would help democratize, and thus build support for, these new energy sources. Today, all American taxpayers fund renewable energy subsidies, but only a deep-pocketed few can cash in on the tax benefits. Publicly traded master limited partnerships and REITs would empower all Americans to invest and have a stake in the transition to cleaner energy.

Renewable energy has come a long way since the 1970s energy crisis but much work remains. We must complement continued technological innovation with critical financial innovation — to level the playing field, incentivize growth, reduce subsidies and democratize America's energy future.

Felix Mormann is a fellow, and Dan Reicher is the executive director, both at Stanford's Steyer-Taylor Center for Energy Policy and Finance.



U.S. SENATOR CHRIS COONS of DELAWARE

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