EXECUTIVE COMMITTEE MEETING TO MARK UP AN ORIGINAL BILL ESTABLISHING ENERGY TAX INCENTIVES

WEDNESDAY, FEBRUARY 13, 2002

U.S. Senate,
Committee on Finance,
Washington, DC.

The meeting was convened, pursuant to notice, at 4:35 p.m., in room 215, Dirksen Senate Office Building, Hon. Max Baucus (chairman of the committee) presiding.

Also present: Senators Rockefeller, Breaux, Graham, Jeffords, Bingaman, Kerry, Torricelli, Lincoln, Grassley, Hatch, Murkowski, Nickles, Gramm, Lott, Thompson, Snowe, Kyl, and Thomas.

Also present: Mark Weinberger, Assistant Secretary for Tax Policy, Department of Treasury; Lindy Paull, Chief of Staff, Joint Committee on Taxation; and Cary Pugh and Elizabeth Paris, Tax Counsels.

Also present: John Angell, Staff Director; Mike Evans, Chief Counsel and Deputy Staff Director; Kolan Davis, Republican Staff Director and Chief Counsel; Carla Martin, Chief Clerk.

OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA, CHAIRMAN, COMMITTEE ON FINANCE

The Chairman. The meeting will come to order.

We are here today to consider tax incentives for energy conservation and production.

It may be useful to remind us why we need these incentives. I think it is appropriate to just think back about a year, when we faced rolling black-outs in California, high consumer prices for gasoline and natural gas, and there were also industrial price spikes that disrupted the economies of a lot of States in the west.

The effects were widespread, they were severe. It was an emergency. I think all agree, the situation is somewhat better now, that that emergency has abated. But certainly our responsibility is not abated.

If we want to do our best to avoid the cycle of repeated energy emergencies, it is our responsibility to do the best we can, knowing it is going to be an imperfect solution, but nevertheless try to enact some provisions that will help ameliorate the possibility of that occurring again.

Tax incentives, I think, can help. They can help achieve energy independence. They are not going to be the sole solution by any stretch of the imagination, but they can help. They can help us conserve. They can help us develop alternative sources, and increased production from conventional sources, in addition.

So, I think it just makes good sense to develop those incentives the best we can to complement the work of the leaders of the Energy and Natural Resources Committee, and also in its own right.

I suggest three principles. The first, is balance. I think we should strike a balance between conservation and production. There is no magic here, but we in the committee, here in the mark, have attempted to strike a balance of about 50/50. That is, half of the incentives for conservation and renewables, the other half for traditional fuels like coal and oil.

A second principle, is technological innovation. We have an opportunity to award the most advanced, the most efficient, productive, new technologies and continue to push those technologies as far and as fast as we can.

The third principle, is responsibility. There is no free lunch. We have said that many times. It is still true today. We must fit our energy tax incentives into a realistic budget.

With that background, let me briefly describe the provisions of the mark. I might add, they were developed with the full participation of Senator Grassley and all members of the committee.

We extend the wind and biomass credit for an additional five years and make geothermal energy eligible as a renewable resource.

We create new incentives for the production and purchase of alternative vehicles. These are the vehicles of the future. They are powered by alternative fuel, by fuel cells, by electric batteries. In the near term, we have hybrids which run partly on electricity and partly on gasoline, but clearly we also want to help in the long term.

We create incentives for the construction of energy-efficient home and commercial buildings, for things like--I have in my hand here a Smart Meter. It is just something new. There are going to be a million other something news.

This is to be hooked onto your electric meter in your home, tied in to your home computer, also to the utility, to program the power coming into your home depending upon the time of day, usage, and so forth, again, to reduce costs and be a bit more efficient.

We create incentives for clean coal. If you retrofit to use currently available clean coal technology, you are eligible for a production tax credit. If you used advanced technology, you are eligible for both an investments credit and also an additional production credit.

We create a new credit for oil and gas production for marginal wells, and a tax break for geological and geophysical expenditures.

We also address electric utility restructuring. This is a pretty important issue for investor-owned utilities, for municipal utilities, as well as for cooperatives. But I must say, there's a lot of uncertainty here, a lot of questions.

I have mentioned the rolling black-outs in California, and many other States have been affected. In my own State of Montana, the legislatures had to delay the implementation of a law calling for a retail choice, and that is because the State does not yet have a competitive marketplace. There is similar uncertainty in other States nationwide.

So my judgment is, at the bottom line, we do not yet know enough about what a restructured electric industry will look like. So, in light of this, the mark calls for Treasury to report back to us by the end of the year on restructuring and tax issues related to it.

The study will help us make the right decisions to address future issues raised by restructuring. At the same time, there are some current problems that we have to address. The mark does so with respect to nuclear decommissioning funds and the treatment of cooperatives.

Finally, we all recognize the enormous potential for development on Indian tribal lands. I have, therefore, included an extension of two provisions in the Code that give businesses an incentive to invest on tribal lands.

Putting all this together, the tax provisions are important in their own right and they will complement the broader energy bill that is about to be on the floor. It is not a panacea, it is a work in progress.

There will be lots of new ideas here in the committee between now and the floor, on the floor, and as we move along. But I think it is a good step. It is solid. It is a step in the right direction.

I also want to very much acknowledge all those who have helped write this mark.

First, the President. The President's budget calls for tax incentives for renewable resources, residential solar systems, alternative fuel vehicles, and combined heat and power systems. They are all included.

Our committee members have also made very important contributions, especially our Ranking Member, Senator Grassley, who worked very hard, and continues to work hard, to make this a balanced bill and a bipartisan bill.

Senator Hatch and others were the principal authors of the alternative fuels provisions. I have been quite impressed with the dedication of Senator Hatch and his knowledge on this subject.

Senator Rockefeller, the principal author of the Clean Coal provisions. There are other members responsible for many other important provisions.

I would like to pay a special tribute to Senators Bingaman and Murkowski. We are lucky to have them on our committee, as the chairman and ranking member of the Energy and Natural Resources Committee, which has the primary responsibility for the energy bill. I thank them for their help and their expertise.

I also thank very much our Majority Leader, Senator Daschle, for bringing energy legislation to the floor and in working with us to make sure that the tax provisions are included.

So, as you can tell, this has been a joint effort. It has been cooperative. The work of every single member is reflected in the mark. I think it is a good start, and I commend it to my colleagues.

Senator Grassley?

OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator Grassley. This is very much balanced between incentives for production, incentives for conservation, and incentives for alternative fuels. That is what we should be doing if we are going to have a real national energy program.

It also makes sure that our energy is affordable, reliable, and clean. In the process, we are helping to guarantee our national security, our economic security, and for individual Americans, personal security.

I am going to put a long statement in the record. I would encourage you, as long as we have 12 or more people here, to move the bill along. So, I will hopefully help by putting my statement in the record.

The Chairman. That is a good precedent, Senator.

[The prepared statement of Senator Grassley appears in the appendix.]

The Chairman. I ask other Senators, and this is the order of appearance: Senator Rockefeller, Hatch, Breaux, Gramm, Graham, Kyl, Bingaman, Thomas, Lincoln, Torricelli, Kerry, Nickles, Thompson, and Murkowski. That is a lot of Senators, all very wise observations.

Senator Grassley. I do not think anybody wants to speak. We just ought to move ahead.

Senator Nickles. Mr. Chairman, I just have one question.

The Chairman. Before the questions, I am going to have staff briefly describe the bill.

Senator Grassley. But very briefly, please.

Senator Nickles. Before you go through the walk-through, I would just ask you, right now, the bill does not have a pay-for?

The Chairman. That is an issue that we have to work out between now and the floor. I think the bill, by the time we get to the floor, should and will have a pay-for.

Senator Nickles. I understand. I understand we are going to mark up the bill. But then I also understand there is going to be a tax increase added after we finish marking it up by the time we get to the floor. I would kind of like to know what that is.

The Chairman. That is not determined yet.

Senator Nickles. In other words, we are going to mark up half the bill, but not the other half of the bill?

The Chairman. We are going to do the best we can with what we have got. The problem is, we have a couple of options. You, Senator, know exactly what they are because we have discussed this, you and I, and also members of the committee.

I think we should have an offset, because otherwise I do not know that we are going to get 60 votes. There is no budget, and 60 votes would otherwise be required.

Once we get through the mark-up and have a committee product, I am going to sit down with the Leader, Senator Grassley, the leadership on both sides of the aisle to discuss our options. But nothing has been decided as of this moment.

Senator Gramm. Mr. Chairman, here is the problem. If we decide the offset here, we have an opportunity to have input on it and have a majority vote on it. If you just make up an offset after we do the mark-up and the bill goes to the floor, then if we object to the offset, it is going to take 60 votes to take it out. I think that is one concern.

A second concern, is we are here talking about cutting taxes because we are the Finance Committee. If we are going to raise taxes, it seems to me the Finance Committee ought to make that determination. Maybe we could have a quick mark-up on it either before we leave for the recess or when we get back.

The Chairman. Well, that is an option that we are going to have to deal with. As I mentioned, Senator Grassley and I are going to talk this over, along with the leadership, again, of both sides. The Senate is going to have to work its will. I do not know what the procedure is going to be, frankly.

Senator Nickles. I would just like for the Finance Committee to work its will.

The Chairman. The Finance Committee certainly, with respect to myself and Senator Grassley, will. I know, preferably, we want the full committee to work its will, but at this point, frankly, because there are Senators on both sides of the aisle very much opposed to offsets, at this time that is not possible. So, we are going to have to work our way through this in a way that does seem possible.

Senator Nickles. Would the chairman yield further? If we make a decision in this committee not to have an offset, I can live with that. But if we are making a decision we are going to mark up the tax cuts, but, oh, incidentally, there is going to be added to this a tax increase, I would like to at least know what that tax increase is and see maybe if it is acceptable or not acceptable.

The Chairman. I appreciate that.

Senator Nickles. The full committee.

The Chairman. There is such division of opinion in the full committee at this point, I am trying to work my way through it until we have more agreement.

Senator Breaux. Use some of that other opinion.

The Chairman. Senator Breaux?

Senator Breaux. Mr. Chairman, I will give you, maybe, the other side of the coin in the sense that the administration has proposed a tax bill provision on the energy bill and they have not proposed any offsets.

The House of Representatives, in fact, I guess, has passed an energy bill with $30 billion of tax incentives with no offsets. Now, I guess this bill is probably, I do not know, around $15 billion. What is it? $15 billion? $18 billion?

Senator Nickles. $13 billion.

Senator Breaux. $13 billion. Somewhere in that neighborhood. I guess we will add it up eventually. But it is in the neighborhood of about half of what the House did.

I would suggest that we follow the recommendations of the White House, follow the recommendations of the Republican House of Representatives, and not do an offset. That is my recommendation.

Senator Nickles. That is fine with me. I am happy to do that, and probably would favor that. I just do not want to find out when we get to the floor, oh, there has been a big tax increase, and we never voted it. Oh, now we have to defend it or we have to have 60 votes to take it out. I would just like for us to collectively decide we are not going to have one or we are going to have one.

Senator Gramm. It depends on what it is.

Senator Breaux. I think we both agree on this. Obviously, if we do not do an offset in the committee, that does not permit anybody on the floor from offering their creation of what they think is the best offset for this bill. Then we cannot stop that.

We can vote against it and vote against it, which I probably would, but we cannot prevent anybody else from offering offsets once the bill gets to the floor. I would recommend we vote against those and just do what everybody else has done.

Senator Gramm. Well, if we could defeat those with 51 votes. But if it is put in it, you cannot get it out except for 60. That is the problem.

The Chairman. Do other Senators have any observations here? I might add, too, that I want to remind ourselves that if there is no offset in this bill, it is going to be hard to get 60 votes. We do not have a budget yet.

Maybe the energy bill is going to be delayed for a while until the Budget Committee meets and there is an allocation made with respect to how the energy bill is paid for. I do not know. I only know, at this point there is no budget. I know that 60 votes will be necessary for the energy bill to pass, because there are no offsets. At this point, this issue is very contentious. I just want to work my way through this until we find a solution.

Senator Torricelli. Mr. Chairman, it just might be helpful if you have a better sense of the membership. I want to express sympathy for Senator Gramm and Senator Nickles' point. It is one thing on the floor if someone attempts to add some offset or this become a vehicle for some degree of taxation and it requires 50 votes.

It is another that those of us who believe that we have authorship of this bill, important provisions of this bill, all of a sudden find out that there is something in it of which we were not authors, but now we cannot get out.

I, for one, joined the Finance Committee because I intended to be involved in tax issues and would like not, instead, to have them imposed upon us by other members. So, I do not know how we resolve this, but I wanted to identify myself with the same concerns.

The Chairman. I would ask Senators, what is their view of knowing that we have that 60-vote budget point of order hurdle? Do they want to phase it? That means it is going to be hard to get an energy bill passed.

Senator Gramm. Well, if we have got a good one, we will get 60 votes.

Senator Kyl. Senator Kyl?

Senator Kyl. Mr. Chairman, I am relatively new to the committee, but the reputation for bipartisan and fairly unified approaches were certainly in my mind when I asked to be a part of this constructive committee.

I think we would have a better chance of having a unified approach, or a more unified approach, if we did have something out of this committee, because all of us would, to some extent or another, be invested in that. I think it could be more easily defended on the floor.

I will give you an example of a concern I have. One of the rumors I have heard, is that Customs user fees would be used. Now, at the very time that we are trying to deal with terrorism at our borders, and I can tell you that we need a lot more money in the Customs Service at the borders, I do not know what we do.

We either increase those fees--and I see lots of people around here who I do not think would want that to happen because of the trade implications--or we use fees that already exist for a different purpose than which they were intended. Frankly, I suspect we need a lot more money for Customs than we are currently appropriating to it anyway, in addition to the fees that it collects.

So nobody would have had an opportunity to go through all of that to figure out how much money we needed and how much Custom user fees could afford to contribute to this, what the effect of an increase on those fees would be.

I just think it would be a lot better if it is identified by this committee and we decide what it is than if we just try to do this on the floor and have to take something out with 60 votes. We would start right out of the box with an effective partisan proposal, and obviously I think most of us would like to avoid that.

The Chairman. These are all very good concerns and observations. Frankly, they are mine, too, as well as everybody's on the committee. I would just ask us to proceed. We will be working with Senator Grassley and, again, the leadership on both sides.

Let us just take this a step at a time. Otherwise, I do not think we are going to get very far. I just urge the committee to proceed with a bill at this point. There have been no decisions, by any stretch of the imagination, made with respect to this subject, or how to, if I determine that I think we should proceed with an offset. There are a lot of questions. You might guess what some of them might be.

I am trying to work it out here with Senator Grassley, again, and the leadership. So I just urge us to proceed with this bill and just take this a step at a time, and we will see where we are. But it will be bipartisan. Senator Grassley and I will agree on whatever it is that we do.

Senator Nickles. If the Chairman would yield further.

The Chairman. Yes.

Senator Nickles. You mentioned it would take 60 votes, or a budget point of order could be made. I would hope that this committee would collectively decide that there is going to be an offset, or there is not going to be an offset. We will stay with you on that 60-vote budget point of order.

Then you have got your 60 votes. You have got 10 people over here, including a couple of people in the leadership, so we could bypass a whole lot of that problem.

Or we could say, hey, we will not make a budget point of order if it does not exceed $13 or $15 billion, and we will do it if it goes above it, or leave that option available. We could do a couple of different things.

What I do not want to see, is have us work for a couple of hours, come up with a package, and then have the Majority Leader stick in something that some of us are adamantly opposed to and say, oh, that is part of the package that we thought was all right. That is not letting the Finance Committee do its job.

Senator Grassley. I assume that we are putting together a bill here that is going to be an amendment to the energy bill, and that it would be a freestanding amendment and the Majority Leader would not intervene the way that Senator Nickles just described. I hope that is the case. Otherwise, I agree with my colleagues.

Senator Nickles. Senator Grassley may have hit the solution. If the Majority Leader or somebody comes on with an amendment on the floor, that is fine. I just did not want somebody to say, here is the base bill. It is in the underlying package and you have to try and take it out, and then somebody make a budget point of order if you do take it out. That puts us very much at a disadvantage.

The Chairman. I appreciate that. As Chairman of the committee, I am interested in other comments by other members of the committee so I can get a better feel of what the wishes of the committee are.

Senator Hatch. Mr. Chairman?

The Chairman. Senator Hatch?

Senator Hatch. How can somebody put something in here, Majority Leader or not, if we pass the bill out of here, except for a technical amendment?

The Chairman. Well, Senator, you know the answer to that question as well as I.

Senator Hatch. You mean, my wonderment is not wonderment at all.

Senator Murkowski. I think the sensitivity, at least on this side, is associated with a couple of things that have occurred. Without generating any spirited debate from the other side, the CAFE issue alone, which is an issue that is going to be debated extensively, was basically removed from the Commerce Committee for an action that we anticipate would be the leaders' amendment on whatever the CAFE number is. To some extent, I think there's been an involvement associated with the Environment and Public Works Committee where there have been some strings that the committee has not been able to resolve that we anticipate. Certainly, as Ranking Member of the Energy Committee, it is no secret that we have not been able to debate, or vote out, if you will, certain aspects of the bill. I think when we get into the electric portion, we are going to find an awful lot of contention in view of the fact that we have not had an opportunity to sort out the details of a very complicated portion of the energy bill in a committee process.

Therefore, you are going to be doing it on the floor and it is going to involve, I think, a fair amount of confusion and pressure on members by special interest groups.

As a consequence, that is why I think we are a little sensitive on this particular issue here to have the potential of the Majority Leader coming in with something that has not necessarily been resolved through the committee process here in its entirety.

So, we have, I think, a legitimate concern. I am anxious to get on with this myself, but I did want to express the concern that I have.

The Chairman. Senator Bingaman?

Senator Bingaman. Mr. Chairman, let me just say, I think under the Senate rules the Majority Leader can call up for consideration whatever bill he wants, essentially. I think all the concerns that have been expressed are certainly valid, and everyone has a right to have those expressed. I hope you and Senator Grassley are able to come up with some bipartisan solution to this issue.

I do think what we can do some good on here in the next hour or so is trying to pass judgment on these proposals that you have brought before us here related to this tax package.

Then, if in fact you determine that we should come back together to vote on the issue of offsets or some particular set of offsets, then that is within your judgment, as I see it.

The Chairman. Thank you, Senator. It is in that spirit that I ask us to proceed. That is, the decision on offsets will be a Finance Committee decision. Senator Grassley and I, in consultation with each, will decide what makes the most sense and perhaps come back together, maybe an amendment on the floor, maybe offered by somebody else.

There are lots of alternatives here. That will be a Finance Committee determination by myself and Senator Grassley. As always--I think almost always--we make joint decisions on these matters, and this will be another one.

Senator Nickles. Just so I understand the Chairman, that is perfectly acceptable. If it is not included in the mark-up today, then it will be done as an amendment to the bill on the floor and not added as the base bill.

The Chairman. I did not say that. I only said that I do not know. I said, whatever the decision is, it will be a committee decision on offsets. It will not be a decision made by others. It will be a committee decision, made by Senator Grassley and myself.

Senator Nickles. Does this committee have 20 members or 2 members?

The Chairman. This committee has 20 members. But by committee, I mean Senator Grassley and I will determine what the next step is. That is, is the next step, as Senator Bingaman suggested as a possibility, coming back and meeting again? Is the next step either ourselves or somebody else offering an amendment on the floor to offset?

One can think of an infinite number of possibilities. But I am just saying that we will decide. It may be our judgment that it is best for the committee to come back again. But that will be a committee leadership decision.

Senator Rockefeller. I think that is a wise decision on your part, Mr. Chairman, and I suggest that we go forward.

Senator Nickles. To clarify, you will have no objection from this side if it is pulling the committee back together to consider it, to amend it, to vote on it, or you will not have any objection whatsoever if you want to do it as an amendment to the underlying bill that we have on the floor?

The Chairman. I can only repeat myself. Senator Grassley and I, working together, will make that judgment.

Senator Lott. Mr. Chairman?

The Chairman. Senator Lott?

Senator Lott. I do not want to rehash everything that has been said, and I apologize for being late, but I was meeting with some people involving the Andean Trade Act.

I just want to say that, first of all, I appreciate the work that you and Senator Grassley have done on putting the package together that we went over the other day.

Obviously, we all might make some changes if we were writing it ourselves, but it is a return to the way we have done business in the past. You have all worked it together and we have all had input, and I commend you for that approach. I think that the substance is worth having, too.

With regard to the issue just discussed, it sounds to me like what you have come up with, what you have said, is reasonable. I was concerned, like everybody else, that we would do our work and then we would find out--in fact, I was very pleased that it did not have a lot of offsets in it, or offsets in it.

If that is going to change, I think you, Senator Grassley, and the rest of us ought to have a chance to have some input on that.

So, I hope now, as you just suggested, we can move forward and report it out the way it is.

The Chairman. What I might suggest, too, at this point, is that we proceed. I think we can dispense with the walk-through. I think members pretty much know what is in this bill. We met yesterday.

There is, however, a modification. I think it only appropriate that, maybe, Lindy, if you are the appropriate person, you explain the modification, because that is new.

Ms. Paull. Thank you, Mr. Chairman.

The Chairman. Then my thought is, it is open for members to ask questions of anyone else before we get to votes.

Ms. Paull. I would just work off of the green sheet. Also, I would note that there is a table before you that we prepared. At the very end, the revenue consequences of each item are shown on the table.

The first set of changes are modifications to items that are already in the Chairman's mark. The first item is to extend Section 45, Electricity Production Credit, to solar energy that is used to produce electricity.

The second item is--

Senator Murkowski. Mr. Chairman?

The Chairman. Yes. Senator Murkowski?

Senator Murkowski. I have a question with regard to Section 45, if I may. It is my understanding that, under this section--

The Chairman. Senator, would you mind if we let Lindy just briefly explain the modification? Or are you asking about the modification?

Senator Murkowski. I am asking about the modification.

The Chairman. All right. All right.

Senator Murkowski. Specifically, that portion. Well, I guess this is in the base bill.

The Chairman. Yes. I think it is. Yes. Thank you.

Ms. Paull. All right. The next modification has to do with the provisions relating to electric vehicles, the Clear Act. The effective date of the proposal in the Chairman's mark would be moved forward to October 1, 2002. It was originally January 1 of 2003.

In addition, there would be a provision that is intended to address Senator Kyl's concern that the qualifying alternative motor fuel vehicles are vehicles that cannot just alternatively operate on the fuels that are available today. They have to be operating on the qualifying alternative fuels.

Senator Hatch. Mr. Chairman, if I could. I appreciate that modification because it was January 1, and now moved to October 1. But I would like you, in conference, to try to even move it closer to the date of enactment, because I think it would make a difference.

The Chairman. Thank you.

Senator Nickles?

Senator Nickles. Lindy, let me ask you a question. I am trying to read this explanation. "For heavy-duty hybrid motor vehicles placed in service before 2003." So, in other words, they have to be placed in service this year.

Ms. Paull. Yes.

Senator Nickles. The allowable credit, $1,000 and $10,000, is increased. Now it would be $3,500 and $14,000.

Ms. Paull. Yes. I mean, there is a schedule in the underlying bill, correct, for these. There are a whole series of schedules in the underlying bill, depending on the vehicle, depending on the weight of the vehicle, the fuel efficiency of the vehicle, and the certain emission standards that are met that determines the amount of credit that would be available. So, there is some acceleration of that schedule in the bill because of this effective date change.

Senator Nickles. Wait a minute. One, the vehicle is already pretty well built, because they have to be in service in the next nine months. So these are things, I do not know if they are already sold or they are close to being sold, but we are just going to increase the subsidy all the way up to $14,000?

Ms. Paull. The ones that we are talking about here are the ones that are meeting the emission standards that would go into effect in the year 2007. So, they are accelerating five years, basically. They are the trucks only.

Senator Nickles. Mr. Chairman, a question. I asked the question the other day when we were looking at some of these vehicles, what percentage of a tax credit, or how much of a tax credit are we getting?

I saw some examples of $2,000 and $3,000, and now I am looking that we go on trucks. I did not know that the allowable credit, I guess under present law, goes all the way up to $10,000. Now we are saying we want the allowable credit to go up on trucks all the way up to $14,000?

Senator Hatch. But those are fuel cell vehicles that are very unlikely to have it.

Ms. Paull. Actually, it is even higher than that. That just happens to be the provision that is being accelerated.

Senator Nickles. How high does it go?

Ms. Paull. For trucks, it goes up to $24,000.

The Chairman. I think it is important at this point, you might explain what size trucks.

Senator Kerry. I think you have to show, not just the size of the truck, but you have to show the concomitant reductions that have to come in the standard.

Ms. Paull. Right.

Senator Kerry. When you have a 2007 standard applied to that, you will begin to see how difficult this will be to achieve and how much of an incentive it is. Can you share that?

Ms. Paull. Well, I do not have the data behind it. But certainly these are trucks that are meeting, five years in advance, the emission standards that will be in effect in five years. So that is a very small category of trucks, and these are the very large trucks.

It is more than 26,000-pound trucks. They are obviously a significant factor. They are on the road all the time. So, this is an encouragement to try to get them to meet the emission standards much earlier.

Senator Nickles. Does the tax credit go all the way up? You mentioned it was much higher than $14,000. I thought that was pretty high.

Ms. Paull. Yes.

Senator Nickles. What is the maximum credit a person could receive?

Ms. Paull. It is a basic amount. This is for the trucks, the big trucks, not the kind of trucks that individuals drive. The kind of discussion that was occurring yesterday with the members had to do with vehicles that were kind of hybrid fuel vehicles that individuals would be purchasing.

Senator Nickles. So passenger cars--

Ms. Paull. We did not really get into the heavy truck issue yesterday.

Senator Nickles. I know. But I am just asking on trucks. Does it go all the way up to $40,000?

Ms. Paull. No. The credit is a basic credit of $10,000. If you meet these additional emission standards and weight requirements, you could be eligible for $10,000, plus the $14,000. So, a total of $24,000 credit.

Senator Nickles. A maximum of $24,000.

Ms. Paull. For the new truck that meets the requirements. That is the early-year amount. Then it declines, the amount of the credit. That would be the maximum. But it declines as you get closer to the required emission standards that all the trucks are going to have to meet.

Senator Hatch. Mr. Chairman?

The Chairman. Senator Hatch?

Senator Hatch. For the alternative fuel vehicles, the maximum credit for a similar, full-sized bus, we are talking about heavy, heavy vehicles that meet 2008 standards now. In other words, you have a tremendous savings.

The amount of the credit is only a fraction of the incremental cost. That is the case for all vehicle categories. The incentive amount reflects only a portion of the incremental costs of the consumer.

Now, when you get down to passenger cars and lighter trucks, the incentives are much smaller.

Ms. Paull. They are much smaller.

Senator Hatch. They are in the $250 to $4,000 range, depending upon the size, the type, and how much fuel savings and environment benefits the vehicle will provide.

But, as a practical matter, the higher priced things are for fuel cell vehicles, and I do not think, as a practical matter, they are going to make it by the end of 2003. But, even if they do, it would be wonderful. If we could get them to do that, it would be a wonderful savings.

The Chairman. Senator Rockefeller?

Senator Rockefeller. I agree very much with what Senator Hatch just said. I think we have to keep our mind, not just on how much the credit is, but what we are trying to accomplish here, which is to make a fundamental shift in the way emissions are handled in this country as a way of lessening our dependency on oil.

A classic example of that. I mean, I have to agree with you on the fuel cell. I commend the President for coming out for that. I thought that was tremendously courageous and, in essence, sort of getting rid of the combustion engine at some point, is what he said.

But on cars, you have got to incent people. You cannot just say, let us clean these things up, and then not give people an incentive. Some of these companies have been making cars and selling them at substantially less than the cost of production as a way of trying to get them into niche markets to get people to buy them. They have been having a very hard time.

So, the tax credit is a way of getting people to create more volume so that, in turn, the price of oil can go down and, as you say, in the out years the incentive will go down.

Senator Kyl. Mr. Chairman?

The Chairman. Senator Kyl?

Senator Kyl. Mr. Chairman, I pointed out yesterday that the State of Arizona had a very unfortunate experience with this alternative fuel subsidy. Since then, we have put the Department of Revenue people from Arizona together with your staff.

Your staff has worked very quickly and very well with them and has made some changes to incorporate recommendations they had based upon their experience back in my home State. Your staff has done a very good job of that. I encourage them to keep on doing that.

One of the problems was the very large amount of subsidy. I think we need to watch that very carefully. Another, was the way the system can be gamed. I am sorry to say that there were a lot of folks in Arizona that figured that out fairly rapidly.

So I encourage other members, if they have questions, to work with your staff, which has been very good about this. I will continue to try to do the same. We have to be very, very careful with this to achieve the proper objective and not open it up for misuse.

The Chairman. Well, thank you very much, Senator. You raised a very good point yesterday, and everyone on the committee realized that and said, hey, we have got to not let that happen. Thank you very much.

Senator Hatch?

Senator Hatch. Mr. Chairman, I will not take long, but I share the concerns of the distinguished Senator. I watched what happened there, and I was supportive of what happened until we saw what happened.

One thing, the incentive Arizona offered made alternative fuel vehicles less expensive than equivalent gasoline vehicles. That led to an unexpected demand and excessive cost to the government.

Then the proposal's incentives are limited to a percentage of the incremental cost of the vehicle. Conventional vehicles will still cost less, even after we give this incentive.

So, that is one difference. Moreover, Arizona's provision allowed incentives for vehicles that did not operate on alternative fuels, and also allowed converted vehicles that did not have to operate exclusively on alternative fuels.

This proposal's incentives are limited to new vehicles that are built to operate only on alternative fuel. No incentive is provided for converting a gasoline or diesel vehicle to an alternative fuel vehicle. I think those changes are going to make this a much more functional thing. So, we hope we have met the Senator's concerns. We are trying to, anyway.

Senator Bingaman. Mr. Chairman?

The Chairman. Senator Bingaman?

Senator Bingaman. Mr. Chairman, the way I am reading this, we are essentially talking about putting a credit in law here for heavy-duty hybrid motor vehicles placed in service by the end of this year.

The Chairman. Right.

Senator Bingaman. With the most optimistic of scenarios, this bill is not going to be signed into law until October.

Ms. Paull. Senator, the original Chairman's mark had an effective date of January 1 of next year. This change moves the effective date to October 1 of this year. That moves it forward three months.

Senator Bingaman. But you get the credit if you buy something between the effective date, which is October.

Ms. Paull. October 1, and the end of the year.

Senator Bingaman. And the end of the year. So there is a three-month period where we are providing an enormous incentive for people to rush out and buy these heavy-duty hybrid motor vehicles.

Ms. Paull. There is still a credit for purchases next year.

Senator Bingaman. Oh, I see. So the credit does not expire?

Ms. Paull. It does, but not for a while.

Senator Bingaman. I just did not detect that from your description.

Senator Gramm. Mr. Chairman?

The Chairman. Senator Gramm?

Senator Gramm. It would help me to know how big these trucks are. I want to know how big of a truck it is that is getting this $24,000.

Senator Hatch. It has got to be over 300,000 pounds.

Ms. Paull. It is over 26,000 pounds.

Senator Gramm. Twenty-six thousand.

Senator Hatch. Or $300,000. Excuse me.

Ms. Paull. So we are not talking about the kind of everyday trucks that individuals drive.

Senator Gramm. Twenty-six thousand pounds.

The Chairman. That is a big truck.

Senator Nickles. Mr. Chairman?

The Chairman. Wait a minute. Senator Gramm, you have the floor. Do you have any other questions?

Senator Gramm. Well, I want to go back and look at that. I think it is very important to figure out what we are talking about. I do not know. Is that a dump truck? Is it an 18-wheeler?

Senator Hatch. First of all, it is a fuel cell truck. Second, it has got to cost well over $300,000. So, it is all on an incremental cost basis.

Senator Gramm. Thank you, Mr. Chairman.

The Chairman. Senator Nickles?

Senator Nickles. Mr. Chairman, I will be quiet in just a moment. But I think I asked what the maximum credit would be, and I think I heard $24,000. Maybe $24,000 is the maximum for hybrid motor vehicles.

Ms. Paull. No. No. That is for these trucks that are over 26,000 pounds. That is the largest category.

Senator Nickles. All right.

Ms. Paull. The kind of vehicles that were being discussed by the committee yesterday were some hybrid vehicles, some of which you may be familiar with because they are on the road now, both individuals purchase them and some businesses do.

They basically qualify for either $250 to a $1,000 credit. Then there is another category of these fuel cell vehicles that also qualify for up to $4,000 of a credit. Then we have various other alternative fuel vehicles.

Senator Nickles. Mr. Chairman, I am looking at the explanation that the staff has. It says, for fuel cell motor vehicles, the credit ranges from $4,000 to $40,000. That is a lot. It says, for automobiles and light trucks, something that we can all comprehend a little easier, the otherwise allowable credit, $4,000 is increased by an amount from $1,000 to $4,000. So right now there is a credit for $4,000, and that would be increased to $5,000, up to $8,000. Is that correct?

Ms. Paull. Yes, Senator Nickles. That is correct.

Senator Nickles. All right. That is what I am trying to find out. I am trying to figure out, how much are we subsidizing? This says, "passenger cars that use fuel cells."

We are talking about increasing that tax credit from $4,000 to an additional $1,000 or $4,000, for $5,000 to $8,000. It also says that there is a maximum credit up to $40,000, which I think maybe we understood it was $24,000. That is a lot of subsidy.

Now, maybe if it is $40,000 and a vehicle costs $300,000, that is one thing. If it is $8,000 for a vehicle that costs $30,000, that is another. That is a big subsidy.

Ms. Paull. The $40,000--and I apologize for not bringing that to your attention because you did ask, what is the maximum credit--is the fuel cell heavy truck, the 26,000-pound truck.

Senator Hatch. Metro bus. A fuel cell Metro bus.

Ms. Paull. The fuel cell heavy truck, the 26,000-pound truck.

Senator Hatch. A fuel cell Metro bus.

Ms. Paull. Fuel cell. Basically, Senator Hatch is right. It is the equivalent of a big bus, like a Greyhound-style bus.

So you can get $24,000 if you are using alternative fuels and the hybrid fuels, and up to $40,000--It will be phased down, though, over this time period--if you use these fuel cells, which is the latest technology

Senator Nickles. But for an automobile, it could be up to $8,000 and the sales price of the automobile may be in the $30,000s. So, you are talking about a very significant portion of the cost.

Ms. Paull. I do not know the sales price of the automobiles.

Senator Gramm. Would natural gas qualify?

Ms. Paull. As an alternative fuel, they do qualify. But the highest of these credits are going after these fuel cell-operated vehicles.21

Senator Thomas. Who makes these fuel cells?

Senator Hatch. Nobody right now.

Senator Thomas. All right. Nobody makes them.

Senator Hatch. It is just theoretical.

The Chairman. Wait. Wait. One Senator at a time. Senator Hatch? Senator Hatch has the floor.

Senator Hatch. Let me just make this clear. You are talking about fuel cell vehicles, and they are not practical right now. We do not have fuel cells fully developed. The President has called for some indication for fuel cells. As I understand it, this subsidy can go up to 2011. For fuel cells, it goes up to about 2006 for hybrid battery and alternative fuel vehicles.

Let us say you could get a fuel cell Metro bus that costs $300,000 to $450,000, and you get the $40,000. It is still less than 10 percent in the final analysis. But the fuel cells are theoretical, but not practical right now.

Now, the hybrids are practical, the battery electric are practical, and the alternative fuels are practical. But fuel cells, it is nice to talk about it, but we do not have that technology.

Ms. Paull. Some of the manufacturers are experimenting with them now.

Senator Hatch. Right. Let us hope we can have it by 2011.

Ms. Paull. They are not commercially available.

Senator Hatch. That is right.

Senator Murkowski. You still need a source of energy for them, though.

Senator Hatch. That is right.

Ms. Paull. Right.

Senator Murkowski. You need propane or some other to basically initiate the process.

Senator Hatch. They have to meet really high standards of fuel savings in order to get this subsidy.

Ms. Paull. Or hydrogen.

Senator Thompson. Mr. Chairman?

The Chairman. Senator Thompson?

Senator Thompson. Could I ask a question? It seems like we are trying to encourage certain behavior here. I think most of us would agree, if something is cheaper you are going to sell more of it, and people will buy more of it. But are we not talking about how much inducement we have to give in order to get what results?

I mean, do we not have to kind of go through a cost benefit analysis with regard to each of these? Trying to decide whether or not a subsidy is too large or too small in the abstract seems to be pretty fruitless to me. It seems to be the question, what do you get for it?

Has anybody ever done a study as to how effective these tax incentives are, or can something like that be done? Could you limit it to a particular kind of item, such as a refrigerator, as we are doing here, or vehicle? Are there other factors involved in the economy or is there a cross-over point? I mean, clearly, this is not hard science.

But it seems to me kind of fruitless to decide, how long is a piece of string. Do we know whether or not there has ever been any studies or analysis as to the effectiveness of the things that we are trying to do here? It seems to me like it is moving in the right direction, things that I think, clearly, we ought to try, and so forth.

The Chairman. Senator Grassley?

Senator Grassley. Lindy, could I answer that?

Ms. Paull. Sure. Sure.

Senator Grassley. He did not ask me. But wind energy, when we passed the Energy Tax Credit in 1992, cost about 7 cents per kilowatt hour to produce electricity by wind. Now we have got that down to about 4.3 cents per kilowatt hour. When we get it down to 3.5 cents per kilowatt hour, we do no have to have the tax credit.

Now, maybe somebody from the industry will come by and say, well, we have got to have it because they want it. But that is what I have been told, that we should not need that after we get 3.5 cents per kilowatt hour.

Senator Thompson. But the removal of the tax credit will have some effect. We do not know what that effect is going to be.

Senator Grassley. No. I am saying it would be economically competitive at 3.5 cents without the tax credit.

The Chairman. Senator Hatch has sought recognition.

Senator Hatch. I think that is a good question. But alternative fuel vehicles and advance technology vehicles, these are hybrids and fuel cells. They significantly reduce the use of gasoline and diesel, and have dramatically reduced emissions. That is the whole purpose of the bill.

Each dedicated natural gas vehicle displaces 100 percent of the gasoline or diesel that otherwise will be used in that vehicle. Today's natural gas vehicles are certified to the California Super Ultra-Low Emission Vehicle Standard, and have no evaporative or running loss emissions. Consequently, manufacturers receive credit for them as advance technology, partial zero-emission vehicles.

Hybrid vehicles combine rechargeable electric systems with smaller internal combustion engines to significantly reduce gasoline consumption.

Now, fuel cells, if we can ever get to the point where they are practical--and we hope we can. That is one reason for these incentives--hold the promise of increased fuel economy, combined with nearly-zero emission levels. That is why this is so important. Conventional gasoline and diesel motor vehicle technology has come about as far as it can in terms of fuel economy and emissions.

The further gains that are needed to allow the U.S. to achieve energy security and clean air, in actuality, require non-petroleum vehicles and hybrid and fuel cell vehicles. We cannot achieve our goals without these vehicles. So, that is the purpose of this bill, and I hope people will support it.

Senator Kerry. Mr. Chairman?

The Chairman. Senator Kerry, did you seek recognition?

Senator Kerry. Yes. Just to hopefully address the Senator's question, and also both Senator Nickles and Senator Gramm, who had questions about this.

In fact, every single aspect of the energy history of this country in coal, oil, and gas, all through history, have been driven by credits. There is $3.2 billion worth of credits in this bill for oil and gas.

There is a credit Senator Murkowski is going to seek which is geared towards the $20 billion cost of the natural gas pipeline, which we have the technology for today. We could build it today, but the cost is the prohibition.

I will join, I am sure, with others here in suggesting that we want to get that done because it is a faster way of getting natural gas out of the Alaska oil shelf to Chicago and distributed to the midwest. That is exactly what we are doing here.

We could not have had the coal industry without some of the subsidies we have had. In fact, the history of almost every tax credit that we have given, not just in this sector but in other sectors, is that it has conditioned behavior. It attracts capital that otherwise will not flow in those directions because of other market costs.

Senator Thompson. The question is, how large should it be, though?

Senator Kerry. Let me just point out, in 1980, when President Carter, in response to the 1973 fuel crisis, put in place a number of incentives, the United States was the world's leader in photovoltaics and alternatives. When President Reagan came in 1980 and took away all of those incentives, we promptly lost the investment in those sectors and Japan and Germany gained the lead.

So, this is a clear opportunity by which we are going to provide an incentive to build something that, even though we may have the technology, people do not find profitable to build unless there is a bottom line that attracts either people to the marketplace to purchase it, or they produce it at a cost that allows them to sell it at a rate that is competitive. It is that simple.

Senator Thompson. Well, you are assuming those incentives have to do with those differing results. I am saying that that begs the question. Are those incentives the only thing, or even the main thing, in the context of other factors in the overall economy? Does anyone have an answer to my question, by the way?

Ms. Paull. Senator, we were just trying to figure out if there was something similar under present law that could have been studied. Certainly, there is a tax credit for electric-fueled vehicles.

I think the answer is, we are not aware of any study that would go into the kind of detail that you are asking for, because I think most people would probably say these tax incentives are going to decrease the price.

People will respond to that, so it would make this kind of a purchase more attractive to them. But it does not go further to say, did we get something for that incentive?

Senator Thompson. What bang for our buck did we get?

Ms. Paull. Yes. That would require a lot more.

The Chairman. Just one more comment. This has been a good discussion. The fact of the matter is, this is a question I asked the staff, too, Senator. There are just no good, solid answers, no solid data on this.

We are just going to have to use our best judgments here, knowing that tomorrow is another day. That is, over the weeks, months, years, as this issue progresses, we are going to be in a position to know what changes we should make, et cetera.

Senator Murkowski?

Senator Murkowski. The objective here is obviously meritorious in trying to reduce emissions. That is the objective. The technology of the fuel cell and its applicability to a vehicle is yet to be developed.

Now, you are talking about an incentive for trucks here as opposed to an incentive for the advancement of the fuel cells so it can be utilized in a truck, or whatever.

Now, that is what is lacking. On the Energy Committee, we have expended about $6 billion over the last decade in developing technology through grants and so forth through the Department of Energy for fuel cells, and everything else. We had a fuel cell in the committee, sitting there percolating.

Senator Gramm. What does it look like?

Senator Murkowski. It looks like an ice box turned sideways. All right.

Senator Gramm. But what is it?

Senator Murkowski. It is a little square box and it makes energy, but it needs a source of energy to make the energy. But the point here is, this is an academic argument, Mr. Chairman.

The Chairman. It is.

Senator Murkowski. Because first of all, while it is meritorious to reduce emissions and have a subsidy, we do not have the technical capability in the fuel cell to put it in a truck. There is no magic to making a truck. They make them all the time. They put gas engines in them, you put diesel in them.

The Chairman. It works on water. It's hydrogen, oxygen, and water, essentially. There is a lot more to it, but you use hydrogen and oxygen and you generate energy.

Senator Murkowski. Like the Stanley Steamer, this is the same thing.

Senator Gramm. It is not like natural gas or propane.

Senator Murkowski. I have got the floor.

Senator Gramm. I am just trying to understand, what is a fuel cell?

Senator Murkowski. You do not have a piston engine.

The Chairman. This is the education of the Finance Committee on energy matters.

Senator Murkowski. In other words, let me finish my point. You can go ahead and pass this, but nobody is going to be able to take advantage of it for a long time because we do not have the technology for putting that fuel cell in a truck and making the truck move.

The Chairman. Senator Hatch?

Senator Hatch. And you are absolutely right. The bottom line is, if they do not meet the standards, the Treasury does not lose any money. If they do, we save a lot on the environment and we start moving towards a more fuel-efficient economy.

Ms. Paull. We have a couple of more items on the modification.

The Chairman. Wait. We need Senators to report this out.

Senator Murkowski. There is an operating hydrogen fuel cell vehicle that has been created. It is a test vehicle. It costs about $6 million.

The Chairman. All right.

Senator Murkowski. This is an effort to try to get the price down. [Laughter].

The Chairman. Senator, I am going to resist to comment on who might be able to purchase one of those.

Senator Kyl. Mr. Chairman? Please, Mr. Chairman, on this point.

The Chairman. Very quickly.

Senator Kyl. There has been no cost benefit analysis. We do not know. That was the problem with the Arizona program. My amendment number six here provides for a GAO study to undertake an ongoing analysis of the effectiveness of the program and to report back its initial conclusions biannually.

The Chairman. All right. We will get to amendments in a second. I would like Lindy to finish walking through the modification, briefly. Then we will get to amendments.

Ms. Paull. The next item in the modification, is the Chairman's mark has a modification to the definition of small refiner for purposes of the exception to the oil depletion allowance. The 50,000 barrel average that is in the Chairman's mark would be increased to 60,000 barrels, average.

The next item, is there is a new tax credit for refined coal in the Chairman's mark. That would be modified to also include high carbon fly ash.

Then the next modification is, there is a study in the Chairman's mark regarding the tax issues resulting from the future electric industry restructuring.

There would be a modification to add into the study language that would ask the Treasury Department to clarify, modify, suspend regulations, look into situations where electric utility company's ability to reorganize is hampered by its capital stock structure.

There are two additions to the package. The first one, is to provide a tax credit for certain residential energy-efficient property. This is 10 percent up to $300. Well, it varies depending on the unit. Excuse me. That is the next one. It deals with various kinds of heat pumps, air conditioners, and water heaters.

The last item is, in addition, a tax credit for energy-efficient improvements to existing homes. There is a tax credit for building energy-efficient new homes, and this would be added on. This is the one that is 10 percent up to $300, basically dealing with energy-efficient insulation materials, exterior windows and doors.

Senator Nickles. Can I ask a question on that last one?

Ms. Paull. Sure.

The Chairman. Yes. Go ahead, Senator Nickles.

Senator Nickles. So if we run down to Home Depot and buy some insulation or special thermal windows, and so on, we get a tax credit as individuals of how much?

Ms. Paull. Up to $300 per year.

Senator Nickles. Is that means tested?

Ms. Paull. No.

Senator Nickles. So we are going to allow Senators to get this $300 tax credit?

Ms. Paull. Well, it is 10 percent of the amount.

Senator Nickles. So if you spend up to $3,000, you get $300 tax credit, all individuals.

Ms. Paull. Yes.

Senator Gramm. Very high energy efficiency.

Ms. Paull. There is a specified energy efficiency in here. There are so many here.

The Chairman. Right. You have to decrease energy consumption in your home by a certain percent. I do not know what it is, but there is a qualification.

Ms. Paull. It is 30 percent.

Senator Nickles. You have to show that you have reduced? How do you do that? If you run down to Home Depot and buy something, do you have to have an energy survey to come by and say this is going to save you?

Ms. Paull. Well, the way this is put together, is that you can either meet a standard that is established by the 2000 International Energy Conservation Code, or you can be certified to achieve at least a 30 percent reduction in heating/cooling energy usage.

Senator Nickles. How do you get certified? Self-certification? This is the Breaux-Nickles. It looks to me like it is very open for abuse. I guess that is kind of the indirect way I am taking it.

I do not know how, with all of the individual returns that are out there, somebody is going to write down a $300 energy savings. How do they substantiate it? Are they going to have to prove it?

Ms. Paull. Well, of course they would have to prove it, just like they have to prove anything else they claim on their tax return.

Senator Gramm. Well, will they not just, at Wal-Mart, put a sticker on high-energy ones and say, "These Qualify?" Is that not how it will work?

The Chairman. Senator Nickles asked a good question. Is there anyone who can answer how one establishes certification here? Does anybody know the answer to that question?

Senator Bingaman. As I understand it, in this we direct the Secretary of Energy to identify the items that would qualify for this kind of a credit. It is like Senator Graham said. If you install one of these, you are entitled to credit. If you buy something else, you are not.

The Chairman. All right. Any other questions on the modification?

Ms. Paull. I think there is also a process for certification that is somewhat, honestly, vague. But there are assorted people that could certify, as well as it qualifying as one of these listed items.

Senator Nickles. Well, I just had some windows put in. You could easily spend $3,000.

Ms. Paull. Yes. I did, too.

Senator Nickles. Do you try to get the window manufacturer or supplier to say, oh, wait a minute This is a thermal window, therefore the Federal Government is going to pay 10 percent of your installation?

The Chairman. Well, we do not know precisely the answer to that question at this point.

Senator Snowe. Mr. Chairman?

The Chairman. Senator Snowe?

Senator Snowe. In response to this issue.

The Chairman. Yes. Yes.

Senator Snowe. Certain standards and criteria have to be met. They are already established. They have been established by the 2000 International Energy Conversation Code. So, there are certain standards in order to qualify.

Ms. Paull. But there is this alternative certification. We are just looking at the statute. It is provided by a third party such as a local building regulatory authority, a utility, a manufactured home production inspection, primary inspection, agency, or a home energy rating organization.

Senator Nickles. So if you spend a couple of hundred dollars to get this thing rated to prove it, you might be able to get your $300 credit?

The Chairman. I would like to proceed here. Senator, if you have questions between now and the floor, I ask you to work it out with the staff and we can clear up any questions that you might have.

If there are no more questions, the modification is hereby adopted. All right.

Any further discussion?

Senator Nickles. What does this last one cost?

Ms. Paull. That one cost $494 million over 10 years.

The Chairman. All right.

Senator Kyl. Mr. Chairman, I just had one question. What was the total cost, with the changes, and the other of the alternative fuel subsidy?

Ms. Paull. The total cost at this point was $14.559 billion, $14.6 billion, over 10 for the whole bill. All of the modifications cost roughly $1 billion to the original mark.

Senator Kyl. So the total is about $15 billion?

Ms. Paull. Just under $15 billion. That is correct.

The Chairman. Other further discussion? Senator Breaux?

Senator Breaux. I have a couple of questions. Shall I do it now?

The Chairman. Sure.

Senator Breaux. It is with Secretary Weinberger. This is an issue that a number of members have been involved in. Senator Graham from Florida, Senator Grassley, Senator Thompson, have also been involved in the question of the use of municipal tax-exempt bonds for pre-paying natural gas supplies for the people for their customers.

We have been working on this since November of 1999. I introduced legislation on this in the 106th Congress, as well as the 107th Congress, to deal with the problem.

The problem, I think, was created back in August of 1999 when the Treasury Department introduced a single sentence in the preamble of a regulation on another matter that indicated that using tax-exempt bonds for this purpose may violate the tax laws. That has put a real dark cloud over the use of municipal bonds for this purpose.

Am I correct, I would ask the Secretary, that the Treasury Department is now prepared to deal with this matter in new rules that would be issued, hopefully, soon?

Mr. Weinberger. Senator, you are correct in the way you describe this provision, how it arose, and that we are going to be coming out with guidance on this. We have been contacted by a number of issuers all across the country, as well as many members of Congress, even some on this committee, as you have identified.

We have reviewed all the comments that have been filed on the issue and met with the affected issuers, and concluded that the municipal electric and gas utilities have a need to secure a firm supply of gas for their customers that, in many cases, is simply not available, absent pre-paying for the supply. The issue faces price risks with respect to the supply they may need to hedge.

So we are actually going to be coming out with guidance shortly on this. We do want to make sure, however, that the prepayment is only at a level that is necessary to provide the services to the customer so that there is no advantage taken of the situation so that somebody can arbitrage. So, we are going to suggest some limits.

We will be coming out with rules shortly, and in those rules we will identify what we think are some appropriate limits, ask for comments, meet with the affected industries and parties before we finalize those limits.

Senator Breaux. But am I correct in assuming that the rules and substance will clarify that municipal or electric/gas systems may use their tax-exempt bonds to fund the prepaid contracts for the purchase of natural gas?

Mr. Weinberger. Yes. What we will say in the rules, is that the issue for municipalities, when they enter into these transactions, is a good business purpose of affirmed natural gas supply and not arbitrage.

Senator Breaux. I know that the last issue that we have had some concern with, and it is a concern to Treasury, is the size of the bond issuance.

Municipalities strongly believe that the limits should relate to the peak needs of the utility so that they can guarantee that they will have sufficient natural gas to heat the homes of their customers on the coldest of the winter days. That issue is of critical importance.

Can you tell us how you plan to try and deal with the issues on the size?

Mr. Weinberger. Obviously, the standard will be the amount necessary to provide reasonable services to the area. That can be determined many different ways. What we intend to do is continue to talk to industry and work out a reasonable standard, then issue it in proposed form so that it will still give people an opportunity to come in and comment on it.

Senator Breaux. All right. Thank you, Mr. Secretary.

Senator Nickles. Mr. Weinberger, could I follow up on that just a tad?

The Chairman. Senator Nickles?

Senator Nickles. I would hope that we would not be in a situation where you would have municipals with tax-exempt buying gas, then reselling it for a profit, competing with others. I do not think that was your intention.

Mr. Weinberger. Senator Nickles, you are exactly right. That is the reason that we were talking about, there has to be a limit on how you can do this so it only is enough to be able to provide a fixed-price contract for serving your area and not an amount in excess of that. That is what we have to work towards.

Senator Nickles. Thank you.

Senator Grassley. Mr. Chairman, I want to associate myself with the colloquy of Senator Breaux. I have had a lot of concern for that same thing in my State, so put me down on his side.

Senator Thompson. Mr. Chairman, I would like to say the same. I appreciate the Treasury's assistance in this matter.

Senator Bingaman. Mr. Chairman?

The Chairman. Senator Bingaman?

Senator Bingaman. Mr. Chairman, I had two items.

The Chairman. Before you proceed, I just want to say, too, I think I can speak for most members of the committee, along with Senators Thomas and Thompson, and Senator Grassley, we are all want care about this.

Senator Bingaman?

Senator Bingaman. Let me ask Mr. Weinberger if he would just comment. One of the problems we have encountered in trying to move forward with any kind of electricity restructuring legislation is that publicly-owned utilities are hampered, as they see it, by these private use rules.

I know you have got some regulations, but they are temporary regulations. There is a great desire to have permanent regulations that they could rely upon to know what their tax status is in this regard. I wonder if you could give us some enlightenment or indicate where you are going to be on that so that we could clarify that, to simplify and move ahead with restructuring.

Mr. Weinberger. I am sorry, Senator. Your question is generally about our position on the proposal in electricity restructuring?

Senator Bingaman. Well, generally. But, more specifically, these private use rules that are in the Code now, and they are seen by publicly-owned utilities as a hindrance to them participating in a competitive market.

Is there a way we could get with the Treasury Department and clarify what the administration's position is before we really get to the floor on this issue so that we could give people a little more confidence that their tax treatment will be something they can live with?

Senator Kyl. Mr. Chairman? Would the Senator from Mexico yield just for a moment on that?

The Chairman. Senator Kyl?

Senator Kyl. I totally support the Senator from New Mexico's position on this, his concerns about it, and might just add one other element to it. The way that I understand the rules are currently being interpreted by Treasury with respect to the allocation of the 15 percent, if it is to equity or non-tax exempt construction, then my understanding is that there is not a problem with the 15 percent private use rule. But, otherwise, there would be. That has at least been offered as one solution to the problem that would otherwise exist, as I understand it, if I am correct.

Senator Bingaman. Yes. I agree with that. Let me add one other thing. There is this additional problem that does not just apply with publicly-owned utilities. That is, with disposing of some of these transmission assets with transmission companies.

What can you tell us about that? Can we work with you to get a resolution of what the tax treatment on that would be and what the administration's position would be on some changes to facilitate that?

Mr. Weinberger. Thank you, Senator. The administration, obviously, as you know, is very supportive of electricity restructuring. We want to do what we can to try to facilitate that.

In that regard, in the vice president's task force and in the president's budget, we do a number of things to try and facilitate electricity restructuring, including encouraging FERC to provide a fair rate of return on transmissions, encouraging FERC to speed up review of rate making, which is a real hindrance to being able to proceed in this manner.

DOE, Department of Energy, has been directed to work with FERC to remove constraints on interstate transmission grids. So, there are a lot of non-tax initiatives we are undertaking.

We have, and are aware, of lots of other issues that have arisen under current regulations and under the tax laws that people have raised that create issues with regard to restructuring. The private use bond rules and the other tax rules that you referred to were written prior to the time for this push towards restructuring.

What we have to do here, is create a balance, obviously. So what we want to do, is encourage the public utilities and private utilities to work together to be able to share assets and be able to have opening up of access so we can have transmissions quickly across the country.

That will require us looking into the definition of private use and seeing how that applies in the context where we are asking public utilities to open up and share their transmission grids with the privately owned and individually owned.

So, we will be revisiting those rules. We are happy to sit down and talk to you as we review them. We certainly realize that we have to see, certainly, how they apply in this context.

One of the difficulties, as you know, is that there has been no clear direction of exactly how we are going to end up economically and directionally with regard to electricity restructuring, so we are trying to conform rules to an unknown quantity.

We want to work with the Department of Energy, we want to work with FERC, we want to work with you all to try and work hand-in-hand to have a policy that is cohesive and a tax policy that does not lead a certain type of restructuring, but rather accommodates a type of restructuring that, from a policy perspective, we all think is the right way to go.

With regard to the transco issues you referred to, whereby I know there have been proposals put on the table in the $4-5 billion range that would change the bond rules, as well as allow certain companies to be able to dispose of assets tax-free, or in certain circumstances, to defer gain on dispositions of assets, particularly as they would be put into these so-called RTOs. We will continue to review those with you. We think they are certainly worth looking at.

We do obviously want to make sure, however, that they are appropriate with the direction that we want to go with regard to restructuring. We will sit down with you in short order to discuss all these issues.

Senator Gramm. Mr. Chairman?

The Chairman. Senator Gramm?

Senator Gramm. On this subject, I think, Mark, here is our problem. It is hard to determine what people's motives are, but I think restructuring is a very important part of this bill and I am for it.

The problem is, there are a lot of people who are saying, look, I have got an REA, for example. Under our bill, we are going to be asking them to basically sell at cost the use of their trunk lines for competition. We are for that. I am for that. Everybody benefits from that, except people who own utility companies.

Now, the problem is, they are saying, oh, but there is a catch here. The catch is, if over 15 percent of my revenue comes from outside of my base payors, which might well happen when I am renting these trunk lines, then I lose my tax-exempt status as an REA or I cannot use tax-exempt financing if I am a municipal. This is not a trivial question. It seems to me that, if we are going to do restructuring, we have got to deal with those problems.

Now, I do not understand this revenue loss. If I am not letting people use the trunk lines, right now, so you are not losing any revenue in the sense that I am not selling the use of it, and suddenly I am selling the use of it, I do not see how you lose revenue.

It seems to me, you lose it relative to what you would have if they did it under the existing Tax Code. But they are not going to do it under the existing Tax

Code. It seems to me, we have made up a revenue problem that impedes restructuring.

You ought to just simply say, well, if people would do these things under the existing Tax Code, we would lose money relative to eliminating these problems. But they were not going to do it under the existing Tax Code, therefore, there is no revenue loss, and kiss this problem goodbye.

Mr. Weinberger. Yes. You are obviously going to a fundamental scoring issue of how we score all of our tax proposals. But with regard to the bond issue that you raise, I mean, obviously the scoring is tied to the fact that you are going to have more issuance of tax-exempt bonds.

Senator Gramm. Say that again.

Mr. Weinberger. You are going to have more issuance of tax-exempt bonds. That is obviously a cost to the government because we subsidize those bonds. That is the score associated with the bond provisions.

Senator Gramm. I do not see how that necessarily follows. If you do not count my renting of the trunk line as revenues against the 15 percent, then I do not lose my tax-exempt status or I do not lose my ability to use tax-exempt financing. How does that change the amount of borrowing I do, unless I borrowed money to build another trunk line? You see, the 15 percent is a problem I have in how I take my revenues.

All I am saying is, exempt the 15 percent from what is counting against my bond, since the 15 percent is arising from competition and I am either transiting electricity across my power grid or I am bringing it in to compete with me. In both cases, America is better off.

Mr. Weinberger. I must admit, I am not fully sure what you mean. The 15 percent issue that you are referring to. Are you referring to the co-op and whether or not you count that in the definition?

Senator Gramm. As I understand it, there are two problems. One, is with a co-op, my tax exemption is based on the fact that 85 percent of my revenues come from selling to my rural customers, the idea being to prevent co-ops from getting into a whole bunch of different businesses.

They rightly ask that, if we now have a competitive system and I am transiting power, and I get paid for it, and that puts me over my 15 percent, how am I affected? I am just saying, all you have got to do is say you are not affected.

Mr. Weinberger. I understand that. That provision is actually in the bill. That is proposed in the bill.

Senator Gramm. That is fixed in the bill?

Mr. Weinberger. Yes.

The Chairman. Yes. We have heard this issue many times.

Senator Gramm. Let me just be sure.

The Chairman. You raised the standard question that was asked by lots of co-ops.

Senator Gramm. Now, so you are saying that is fixed for the REA. Now, what about fixed with regard to the municipal that has the ability to use tax-exempt financing?

Senator Kyl. Mr. Chairman, I think it is 10 percent in that case, not 15 percent.

Senator Gramm. All right. It is 10 percent. All right.

Now, what about their problem? If they go over 10 percent as a result of renting the line, is that fixed in the bill?

Mr. Weinberger. No.

Senator Gramm. Well, why do we not fix it?

Mr. Weinberger. That is something we will explore. That is what I think Senator Bingaman raised, Senator Kyl raised. I think we want to sit down and see how we want to do it.

Senator Gramm. I am just saying, if we fixed it we could get more votes for restructuring, which I would like to do. I mean, that would be something we could do that would be good for the country. Good, in a macro sense. Good for everybody, every consumer.

I really think, Mark, if you looked at that and if you could give us a way of fixing it and we could agree on a bipartisan basis, we could get more votes for restructuring.

Ms. Pugh. Senator Gramm, if I could add, there are temporary Treasury regulations that address the tax-exempt bonds. There are temporary Treasury regulations that address the treatment of the municipalities.

Senator Gramm. I do not want the municipalities to be able to use tax-exempt bonds to produce energy to sell competitively somewhere else. I am not for that.

But I do not want--and I misspoke myself. I had gotten on the 15 percent with REAs--the leasing of lines to drive them above their 10 percent threshold and deny them the ability to use tax-exempt financing for what they are already doing.

I think there is a problem if we let either REAs or municipals use tax-exempt financing to compete against other power companies in selling power somewhere else. I am not for that.

But I just do not want to get in a position where every REA, many of whom are not for competition, or every municipal, many of whom are not for competition, to have this convenient excuse.

People are moved by these excuses. So if we could deal with that problem, and I will stop, Mr. Chairman, I think it would be very helpful. If our goal is to have a restructuring plan, I think it would help promote it, if we could. I feel better knowing the REA thing is fixed.

Senator Kyl. Mr. Chairman?

The Chairman. Senator Kyl?

Senator Kyl. I really subscribe to everything Senator Gramm just said. Senator Bingaman is really the one who brought this up, but we have the same issue here. My understanding is that, if the Treasury regulations were made permanent, that would solve at least this part of this particular problem. So, that is one way that it could be solved.

Another way, is that we could deal with it legislatively. My understanding is that Joint Tax just has not had the time, with everything else, to determine whether the proposal is the right way to do this, would work right, score right, and so on.

I would hope that, between now and the time we get to the floor, we could determine that so that if there is a fairly easy fix here along the way that we have talked about, we might be able to achieve that.

Finally, to the point about more tax-exempt bonds. Actually, I think you are going to see a lot fewer. The reason is, the municipals now can finance a lot of their system with tax-exempt bonds because they are serving their own load.

But now with competition, there is going to be a lot more of the so-called private use. Their transmission is going to be used a lot more for that and they are not going to be able to use municipal bonds for that purpose. So, my guess is, you will see a lot less of it rather than more of it.

Mr. Weinberger. Mr. Chairman, I am sorry. If the 10 percent issue that you raised, the 10 percent private use, if you use more than that you run afoul of the private use rules, that is a statutory provision so that does require a statutory change.

Senator Gramm. No. I know. We are in the statutory business.

Mr. Weinberger. We also talked about the regulations.

Senator Gramm. We are changing all kinds of statutes here.

The Chairman. Well, I think Senator Kyl made the main point. Let us look at it between now and the floor.

I think Senator Thomas has an amendment.

Senator Thomas. I do have an amendment, Mr. Chairman. Thank you. I am joining with Senator Rockefeller, Senator Breaux, and Senator Hatch in this. It has to do with Section 29, which has to do with non-conventional sources of oil and gas.

The Chairman. This is amendment number 50? That is my understanding, that this is amendment number 50, for the information of all Senators.

Senator Thomas. All right. This was prepared yesterday after our mark-up, so we forwarded it to the Joint Tax Committee last evening. I wonder if Lindy would like to describe it to us, please.

Ms. Paull. Yes. Thank you, Senator Thomas.

It is my understanding, the way this amendment would work, is that it would restart Section 29 on the date of enactment for new facilities, generally. The amount of the credit would be set at $3, and there would be no inflation adjustment. The maximum is $3 per barrel, or BTU oil barrel equivalent.

The kinds of things that would qualify, would be the same things as present law, except for synthetic fuels produced from coal. Then it would be expanded to also include viscous petroleum and coal mine methane gas. There are so many of these, coal mine, coal bed. But this is coal mine methane gas.

There is a special rule for the coal mine methane gas in the sense that the new facility rule does not really work for that. So, the coal mine methane gas would just be given the credit for, in essence, almost three years. There would be a three-year placed-in-service date and the credit would be of a three-year duration.

Senator Thomas. This is not a new program. It has been in place before, and it has expired. It is coal bed methane, as well as shale and tar sands. It is simply designed to get these non-conventional sources of energy into an economic, producing fashion and bring it back to where it has been before for a period of time.

Senator Rockefeller. Mr. Chairman?

The Chairman. Senator Rockefeller?

Senator Rockefeller. This has been around for a long time in the committee and has a long history. It is a way of getting at the non-conventional sources. In my part of the country it would be called Devonian shale, in your part of the country it would be called something else.

Senator Thomas. Coal bed methane.

Senator Rockefeller. Yes. And coal bed methane is extremely important. It is three years. It is limited. It makes sense. The committee staff liked it, the

Chairman appears to like it, and it is an important thing to do. It is only for new wells. If you do not have it, you do not drill new wells. There is no incentive, because it is unconventional.

The Chairman. Senator Gramm?

Senator Gramm. The question I had, and maybe Senator Rockefeller answered it, but let me ask the staff. Is this prospective? Will any current production get any benefit from this or will it all be new production?

Senator Rockefeller. No. New.

Senator Thomas. All new. All new.

Ms. Paull. It is basically all new. The one little bit of a wrinkle on this is the coal mine methane, which could be extracted from an existing mine. You could be extracting it before you drill a mine. The notion of a mine does not work as well for that, we think.

Senator Thomas. This is not a goal mine. These are wells that are drilled on top of a coal bed and the gas is down between the water and the coal bed. It is not a mine. These will be new wells.

Ms. Paull. These will be new drilling and extraction of it.

Senator Gramm. My question is, if I have already got the project and it is already producing, do I get the benefit or does it have to be a brand-new project? What does the language say?

Senator Rockefeller. New. New.

Senator Gramm. If it is a brand-new project, I think it is stronger.

Senator Rockefeller. It is, specially.

Ms. Paull. It is a brand-new project.

The Chairman. Wait. Wait a minute. People are jumping in. Let us get the facts here. We are talking about coal mine methane, and somebody else is talking about coal bed methane. Lindy, could you distinguish the two with respect to the question raised by the Senator from Texas?

Ms. Paull. For everything else, it is new. The coal mine methane is new extractions of it, but there could be an existing mine involved.

Senator Gramm. But the mine is not producing methane now, nor has it ever produced methane.

Ms. Paull. Well, in order to be able to work with the mine, you have got to get the methane out, apparently.

Senator Rockefeller. And it is not drilled.

Ms. Paull. You know more about this than I do.

Senator Rockefeller. It is not drilled, it is released. It is the thing that blows up mines. You have got to get rid of it.

Senator Bingaman. Mr. Chairman, as I understand it, this coal mine methane comes out of mines at the current time.

Senator Rockefeller. Yes.

Senator Bingaman. What we are trying to do is provide an incentive for it to be captured as fuel.

Senator Rockefeller. Yes. And used.

Senator Gramm. What I am asking is, to get this credit you cannot be capturing it now, right?

Senator Bingaman. No. That is right.

Ms. Paull. They are not capturing it now and getting a credit.

The Chairman. Senator Murkowski?

Senator Murkowski. This is not limited to coal bed methane.

Ms. Paull. That was just one of the expansions that I mentioned. It is basically what would qualify for the Section 29 non-conventional fuel credit today, except for, synthetic fuel would not qualify, even though it would under present law. It would be expanded in two ways, the coal mine methane and, I refer to it as heavy oil, but the viscous oil.

Senator Murkowski. What is the viscosity of the heavy oil to qualify?

Ms. Paris. Twenty-two degrees API.

Senator Murkowski. Twenty-two.

Ms. Paris. Right.

Senator Murkowski. Now, it is my understanding that there was some consideration relative to States that might have that. I think Arkansas has some, California, we have some, other States. This oil has been in place, but the economics of lifting it, under the current price structure, have made it impractical.

Now, the purpose of this credit is to encourage that domestic recovery. You have limited this now to three years. I do not know what your scoring is, but that is an awfully short time for the technology and the commitment to go in and try different types of recovery methods and try and amortize them. I was under the impression that we were talking about five years, and it has been cut down to three, is my understanding. Is that right?

Ms. Paull. That is correct, Senator.

Senator Murkowski. And the rationale behind that is scoring?

Ms. Paull. I think we were given a budget.

The Chairman. Revenue. Revenue.

Senator Murkowski. Well, we were given a budget. It is kind of hard to figure out just where that came from. But it is a $3 credit.

Ms. Paull. It is a $3 credit, with no inflation adjustment.

Senator Murkowski. No inflation, no tax, no nothing.

The Chairman. I think we have pretty well discussed this.

Senator Breaux. Mr. Chairman?

The Chairman. Senator Breaux?

Senator Breaux. I would just point out, because we had a discussion of whether it was for existing wells that are now subject to the Section 29 credit, and it is not. It is only for new production after the date of enactment, does this apply.

The House bill, on the other hand, covers existing wells that were subject to the Section 29, as I understand it, which obviously makes it much more expensive, about $3 billion, than the House bill. We were operating with $1 billion.

That is why it is only prospective, and that is why it is only three years instead of five. We are going to have to go to conference on this, and somewhere between the two you will probably find the ultimate answer.

The Chairman. Further discussion?

Senator Bingaman. Mr. Chairman?

The Chairman. Senator Bingaman?

Senator Rockefeller. Senator Bingaman is also a sponsor of this.

Senator Bingaman. I support what we are trying to do here on Section 29. I wanted to raise one other issue. Is this the right time to do it?

The Chairman. No. We are on 29 right now.

Senator Thomas. I am sorry. Senator Bingaman is also a co-sponsor. I did not know that.

Senator Nickles. I am, too.

The Chairman. It sounds like there is a lot of support for this issue.

Senator Nickles. Mr. Chairman?

The Chairman. We are about to vote, but go ahead.

Senator Nickles. Mr. Chairman, I am not going to object to this. But if people talk about trying to adopt the House provision, which reaches back on existing wells that have already had 10 years, that would be a serious mistake.

The Chairman. We are not. We are not doing that.

Senator Nickles. This subsidy is enormous. It is over $6 a barrel equivalent on oil, and I think about $1 on gas. I am no going to object. If you reach back on the old, the old 29 subsidies are enormous. It is a serious mistake.

Some people want to extend those forever, and we should not do that. It is enormously expensive, plus it makes us choose, this well is good, this well is not. We should not be doing that. I am not going to object on this extension for three years at $3, fixed. But if we are going to start expanding this, there are going to be serious objections.

The Chairman. Well, I think there is a lot of support in the committee for extending 29, albeit on a scaled-back basis, which this is. Without objection, the amendment is agreed to.

Senator Thomas. Thank you, Mr. Chairman.

Senator Lincoln. Mr. Chairman?

The Chairman. Senator Lincoln?

Senator Lincoln. Mr. Chairman, I have an amendment. It is number 24.

The Chairman. All right.

Senator Lincoln. Mr. Chairman, I am pleased to be joined by Senator Grassley in offering an amendment to provide tax incentives for the production of biodiesel from our agricultural products.

The amendment provides a partial exemption for the diesel excise tax for diesel blended with biodiesel. Specifically, the amendment provides a one cent reduction for every percent of biodiesel blended with diesel, up to

20 percent. Joint Tax has scored the amendment at less than $100 million over 10 years. Is that correct?

Ms. Paull. That is correct.

Senator Lincoln. The amendment also contains provisions for the reimbursement of the Highway Trust Fund from the USDA Commodity Credit Corporation, the CCC, to protect the trust fund from lost revenues due to the biodiesel incentive. The cost to the CCC would be offset, at least initially, by the savings from the marketing loan program.

With today's depressed prices from farm commodities, we have just gone through a long discussion on the floor, biodiesel has been identified as a ready new market for our farm products. Even after years of research and market development, biodiesel is not yet cost competitive with petroleum diesel. In order to do so, market support and tax incentives are much needed.

The provisions provided in the amendment will help in leveling the field for biodiesel blends and help jump-start this exciting new industry. It is very user-friendly, and environmentally it provides great benefits.

The time is ripe for investment. It is ripe for our economy, it is ripe for our environment, and our national energy security. So, I urge my colleagues to support the amendment that is offered by myself and Senator Grassley.

Thank you, Mr. Chairman.

Senator Grassley. Mr. Chairman?

The Chairman. Senator Grassley?

Senator Grassley. She said all that can be said about it. I have not said it yet, and I am not going to. But I hope you will support this. One additional thing, is the environmental value of soy diesel.

When we reach the environmental goals of getting sulphur out of diesel, that sulphur, today, even though it is environmentally harmful, does serve a useful product in the diesel. Biodiesel will help take the place of that as well.

Senator Breaux. Mr. Chairman?

The Chairman. Senator Breaux?

Senator Breaux. The amendment is described as providing a tax credit for the production of biodiesel from virgin agricultural oils. Do we have a definition of "virgin agricultural oils?"

Senator Lincoln. I do not, but I guess it is new. It is obviously something we produce annually.

Senator Breaux. It is probably in here somewhere.

Senator Lincoln. Yes.

Ms. Paris. Senator, to clarify, that is not recycled.

Senator Breaux. All right.

Senator Gramm. Mr. Chairman?

The Chairman. Senator Gramm?

Senator Gramm. Mr. Chairman, this is the way we got into the whole ethanol thing. Soybean has many good uses. It is a valuable product. Why we should be providing massive subsidies to use it for something else, I do not understand.

The subsidy looks small when you compare it to a gallon of diesel, but when you look at the additive and how small a percentage that is, the subsidy for basically taking soybeans and turning them into a diesel additive is huge. I am opposed to it and I would like the opportunity to vote against it.

The Chairman. Any discussion?

Senator Lincoln. I would just like to answer the gentleman from Texas. Soybeans and other products do have a lot of great uses, and we may see more production of those commodities, depending on what happens in the outcome ultimately of the farm bill.

But I would just say, about any agricultural oil, including the oils from soybeans, cottonseed, or rice, is completely renewable. Also, from the standpoint of soybeans compared to ethanol, yes, we are trying to put it into the perspective of what we have done with ethanol, but soy diesel is much more user-friendly. You do not have to clean the pipes. It is transportable. It is certainly much more practical in the end in terms of an alternative fuel.

I think it is a very practical way to look at encouraging something that I think, because of the research we have, is probably much more likely to be usable sooner in a more practical way. I hope the gentleman would reconsider.

It is obviously biodegradable and non-toxic, and it is the first and only alternative fuel that meets the EPA Tier I and Tier II health effect testing standards. So, it has already made half the journey and I think it would be a good substitute.

Senator Nickles. Mr. Chairman, could I ask a question?

The Chairman. Senator Nickles.

Senator Nickles. Correct me if I am wrong, maybe staff or Senator Lincoln, but ethanol gets a subsidy of basically about 5.3 cents a gallon. As I understand it, this could go up to 20 cents per gallon?

Senator Lincoln. I think, when you look at the cost of where you have gotten the production of ethanol, ethanol is roughly--and I do not know--but about $1.50 to $1.60.

Senator Grassley. Retail.

Senator Nickles. I am talking about the subsidy per gallon.

Senator Lincoln. Right. But the problem is, because we have not focused on biodiesel, and because we have not looked at it as an alternative, it has not had the kind of investment or the exposure to be able to bring down that price and make it competitive, even though it is unbelievably competitive for all of those reasons. It is more user-friendly in the pipeline. It is easily mixed.

Senator Nickles. Would the Senator be willing to modify your amendment to say the subsidy shall not exceed the per-gallon subsidy that gasohol gets, or ethanol gets? I just think 20 cents a gallon is ridiculous. Ethanol is awfully high at 5.3. When I read something that says it is a maximum credit of 20 cents per blended gallon of fuel, I just think that is way too high.

Senator Lincoln. I think ethanol is actually higher than we are. I am not sure.

The Chairman. Ms. Paris? I see you wanting to jump in here. What do you want to add to this?

Ms. Paris. I apologize for interrupting. The total amount of the credit currently is 53 cents per gallon, and it is scheduled to decline to 51 cents per gallon. I think the 5.3 number that you are referring to is probably the 4.3 number that is currently part of the Highway Trust Fund.

The Chairman. No, no. No.

Mr. Weinberger. No. The 5.3 is for gasohol and the 53 cents per gallon is for ethanol.

Senator Nickles. Right. So 53 cents per gallon of 100 percent ethanol, and 5.3 cents per gallon of the 10 percent blended. But the blended diesel that you were talking about, soy diesel, would be 20 cents per gallon subsidy of blended. Am I correct? I think that is four times as much, on a blended basis.

That is too much. I mean, everybody is just coming up with amendments. We are trying to design cars and offer all kinds of subsidies. Now we are designing fuel and we are talking about subsidies four times as much. I think that is awfully high. Per blended gallon, 20 cents is an awfully big subsidy.

Senator Lincoln. But it is higher already.

Senator Grassley. The traditional relationship that a farmer gets for a bushel of beans is usually three times--not right now, but usually over the long history--that of corn. We ought to reflect that ratio in the price that she is telling you here.

Senator Gramm. Mr. Chairman?

The Chairman. Senator Gramm?

Senator Gramm. I think the fact that the price is higher is a good reason that we ought not to be burning it up.

Second, we do not even know if you use more energy in making this stuff than you gain. This may be a net energy-using activity. As you know, there has been extensive scientific debate about whether ethanol actually uses energy or saves energy.

Senator Grassley. You are 10 years behind on ethanol, except for a bunch of humanitarians that think you should not use food for anything but for people to eat.

Senator Gramm. All I know is, there are a lot of people in the scientific community who still debate that about ethanol. It is getting one-fourth the subsidy.

Senator Lincoln. Would the gentleman yield?

The Chairman. We are kind of going around the flag pole here.

Senator Nickles. Mr. Chairman, I think I can help clarify a couple of things.

The Chairman. Senator Lincoln?

Senator Lincoln. We never get 100 percent out of any fuel that we burn, or that we use. But if you look at where ethanol has been and where it is now, I think if you make the comparison, it at one time obviously cost more to produce than it was effective or competitive as well. Yet, we have been able to work to make it more competitive in terms of cost.

The Chairman. Senator Nickles has the last comment here.

Senator Nickles. Mr. Chairman, I think, to clarify the amount of subsidy, ethanol gets 5.3 cents on every blended gallon, assuming it has 10 percent ethanol, or 53 cents if it was 100 percent ethanol. The blended portion that you have is one cent for each percent.

So if you had 10 percent identical to the same requirement as ethanol, it would be 10 cents. So, the subsidy would be double if you had the same blended rate as ethanol. Your amendment also says you can go up to double that amount.

It could be blended up to 20 percent, therefore, you would have four times the subsidy that ethanol has. I think it is too generous. I would hope that you would say that the maximum subsidy would be equal to, on a blended basis, of no more than 5.3, or the same thing as ethanol.

The Chairman. Is there any further discussion?

Senator Nickles. Would you be willing to modify it?

Senator Lincoln. No, sir, because it costs $2.50. It is so much higher to make at this point because we have not had the benefit of what ethanol has had. We have got to get it to that mark in order to be able to do that.

The Chairman. All right. We have had this discussion now.

Senator Grassley. You have got to mix it at 20 percent.

The Chairman. All right. All those in favor of the amendment, say aye.

[A chorus of ayes]

The Chairman. Those opposed, no.

[A chorus of nays]

The Chairman. The ayes have it. The amendment is agreed to.

Senator Gramm. We would like a roll call vote.

The Chairman. All right. The Clerk will call the roll.

The Clerk. Mr. Rockefeller?

Senator Rockefeller. Aye.

The Clerk. Mr. Daschle?

The Chairman. Aye, by proxy.

The Clerk. Mr. Breaux?

Senator Breaux. Aye.

The Clerk. Mr. Conrad?

The Chairman. Aye, by proxy.

The Clerk. Mr. Graham of Florida?
Senator Graham. Aye.
The Clerk. Mr. Jeffords?
Senator Jeffords. Aye.
The Clerk. Mr. Bingaman?
Senator Bingaman. Aye.
The Clerk. Mr. Kerry?
Senator Kerry. Aye.
The Clerk. Mr. Torricelli?
The Chairman. Aye, by proxy.
The Clerk. Mrs. Lincoln?
Senator Lincoln. Aye.
The Clerk. Mr. Grassley?
Senator Grassley. Aye.
The Clerk. Mr. Hatch?
Senator Hatch. Aye.
The Clerk. Mr. Murkowski?
Senator Murkowski. Aye.
The Clerk. Mr. Nickles?
Senator Nickles. No.
The Clerk. Mr. Gramm?
Senator Gramm. No.
The Clerk. Mr. Lott?
Senator Lott. No.
The Clerk. Mr. Thompson?

Senator Thompson. Aye.

The Clerk. Ms. Snowe?

Senator Snowe. Aye.

The Clerk. Mr. Kyl?

Senator Grassley. No, by proxy.

The Clerk. Mr. Thomas?

Senator Thomas. No.

The Clerk. Mr. Chairman?

The Chairman. Aye.

Senator Grassley. For what is worth, we picked up two votes of people that voted against ethanol and lost the votes of two people that had voted for ethanol.

The Chairman. All right.

Senator Bingaman. Mr. Chairman?

The Chairman. Senator Bingaman?

Senator Bingaman. I had two items I wanted to mention. First, there was a paragraph of report language that I hope we could add to our report related to this municipal issue that we had the discussion about. I hope it accurately reflects what we discussed here and what the committee's consensus is on that.

Is that something you have had a chance to look at?

Ms. Paull. We took a quick look at it. I think our staffs have talked about a few little modifications to it.

Senator Bingaman. All right. That will be fine. I hope we can include that, Mr. Chairman.

The one other thing, is I have an amendment that is item number 18.

The Chairman. Before you proceed, I neglected to let the Clerk announce the result of the roll call.

Senator Bingaman. Oh. All right.

The Clerk. Mr. Chairman, the tally is 16 ayes, 5 nays.

The Chairman. The amendment is agreed to.

Senator Bingaman. It is the amendment numbered 18 which relates to a credit for manufacturers of energy-efficient new homes.

As I understand it, the Chairman's mark has a credit in it for energy-efficient new homes. What I am trying to do, is to just modify the language so that we also make that available for manufactured new homes in a practical way, which means that essentially they would use the Model Energy Code as the benchmark for manufactured homes and have to qualify for the Energy Star designation. Is this something we could work on between now and the floor to try to get this provision?

The Chairman. I would say to the Senator, the answer to that is, yes. We do not have a score.

Senator Bingaman. Yes. It does not score.

The Chairman. Let us see if we can work something out.

Senator Bingaman. I think it is an important provision. Thank you very much.

Senator Gramm. I think it makes good sense and we ought to do it.

The Chairman. Senator Murkowski?

Senator Murkowski. Mr. Chairman, I have an amendment. I think it is number 28. What it is, is a payback provision. We discussed it yesterday during the meeting. In order to encourage the development of some of our clean, natural gas that is some 3,000 miles from the market, the proposal is to give a $3 tax credit.

Now, we have already done this for coal relative to tax credits. The way this thing would work, and I believe there would be very little, if any, revenue lost, is it would be structured so that when the price of gas, say, exceeds $3.75, any tax credits that were previously claimed would have to be refunded to the Treasury.

Thus, say in the year 2010, if the price of gas were $3.50, the owners of the gas would receive a 25 cent credit. If the next year the price of gas was $4.10, the owners would have to refund the 25-cent tax credit they claimed in the prior year.

As I indicated, we have got tax credits for hybrid vehicles, energy-efficient natural gas fueling stations. This would provide a cushion, if you will, for the producers who are looking at something in the area of $20 billion in the project associated with bringing this gas to market. With the fluctuations of gas, there is a certain amount of uncertainty.

On the other hand, the realization that we are pulling our gas reserves down faster than we are finding new ones suggest that this is not going to be a liability for the Federal Government. Now, we have asked for a scoring and I do not know what you have come up with, Lindy, on this.

Ms. Paull. Senator, we are feverishly trying to work on this score. This is something we have not scored before, so we would ask that you give us a little bit more time to work on it.

Senator Murkowski. I would like to have it included in the mark. It has a provision of a payback. So we are not talking about a situation that is wide open from the standpoint of a subsidy or a contingent liability for the Federal Government, because when the price of gas goes over it kicks back in and pays it back.

Ms. Paull. Yes, Senator. This is a fairly complicated proposal.

Senator Murkowski. It is pretty simple in the sense that we are going to pay it back. It is not like a normal subsidy that you are looking at for three to five years.

Senator Gramm. Mr. Chairman?

The Chairman. Senator Gramm?

Senator Gramm. Mr. Chairman, I am opposed to this amendment. I think we are starting down a very slippery slope here where we are going to set a floor on the price of a commodity and we are going to set a ceiling on the price of the commodity.

We have not the foggiest idea of what it is going to cost because we do not know what is going to happen to the price of natural gas. There are many new areas of development, many new products. I think this is bad public policy.

I understand why the Senator is for it. I would like to see the reserves in Alaska developed. But I do not know of any other way to do it efficiently other than to have it done when the market dictates that it is done. Natural gas prices today are pretty good.

I think we are just committing ourselves to something that we do not understand and we do not have any idea of what setting this floor is going to do, nor do we have any guarantee that setting a ceiling will recoup a similar amount of money.

I think, if we believe that resources ought to primarily, except under the most extraordinary circumstances, be allocated by price, then I think we have got to be against something like this.

Senator Murkowski. If I could respond.

The Chairman. Senator Murkowski?

Senator Murkowski. Let me suggest to you that there is no ceiling on here. There is a floor and there is a payback provision.

Senator Gramm. The payback is the ceiling. Above that level, you start paying it back. Right?

Senator Murkowski. Well, yes. But it is not like you would have a range. It is whatever the existing market is, vis-a-vis a well head of a $1.25, plus transportation.

As the price goes up, why, if it goes over that, then there is a payback. It is not like most of these open subsidies where, clearly, there is a subsidy for an extended period of time.

This is an extraordinary project in the sense that you are looking at a $20 billion project that is going to move about six billion cubic feet of clean gas into the domestic market each day.

It is going to do a lot to basically offset the gas that is being pulled down as a consequence of the large reserves that we are pulling down faster than we are finding new ones. There is nowhere else in the United States where there is a proven reserve of the magnitude of 36 trillion cubic feet of gas.

The question is, how can we bring this to market? You are not going to bring it to market without some kind of provision because of the risks associated with the investment. We are not asking for an unreasonable risk to be assumed here.

We are talking about a payback for that risk because we know, over an extended period of time, the price of gas is going to go up to the point where it will pay back whatever it was down to to offset that differential.

The Chairman. Senator Breaux?

Senator Breaux. I noticed that the amendment is based on the price of gas at the Henry Hub. I imagine not too many people know where the Henry Hub is.

Senator Nickles. It is right next to the Henry Pub.

Senator Breaux. Yes. It is in Louisiana, and that is exactly, probably, what it is.

But I think the amendment is really good. I mean, I think that we have gas wells that are being drilled in the Gulf of Mexico that are over 1,000 feet deep. The same argument would apply to that hard-to-find natural gas. It is also very expensive, sometimes prohibitively expensive. They are not going after the really deep-water stuff because it is simply too expensive to bring it in through a pipeline.

So, I appreciate what the Senator is doing for Alaskan gas. But the same argument applies to gas in the deep waters of the Gulf of Mexico, where most of the natural gas comes from.

I think if you start saying, we are going to give a tax credit for expensive gas coming from over here, but not anywhere else, it does not seem like it makes sense. It is not good national policy, I think.

Senator Murkowski. Do you not, though, enjoy a deep-water royalty relief in the Gulf?

Senator Breaux. Not enough.

Senator Murkowski. Well, I know it may not be enough, but it is pretty significant. That deep-water royalty relief is ongoing. There is no payback associated with deep-water royalty relief. This is a payback. We are not asking for a subsidy.

Senator Gramm. You do not pay it back.

Senator Murkowski. Sure you pay it back.

Senator Bingaman. Mr. Chairman?

The Chairman. Senator Bingaman, and then let us wrap this discussion up. I understand that the Senator is not going to offer his amendment. This is a very helpful discussion.

Senator Murkowski. The amendment is before us.

The Chairman. Oh. You are not going to withdraw it?

Senator Murkowski. No.

The Chairman. All right. Senator Bingaman?

Senator Bingaman. Mr. Chairman, let me just say, I certainly agree with the intent of what the Senator from Alaska is trying to do. I do think this is a unique circumstance where you have got an enormous reserve of natural gas. We are not able to get it down to where we need it in the lower 48.

We need to find a way to provide enough confidence so that the capital will flow to construct this pipeline. There is enormous volatility in the price of natural gas, and this would help to compensate for that.

Now, I do not know about the particular formulation that he has come up with here. Frankly, I think we need to study that to determine whether that is the right formulation.

But I favor putting in place whatever we can in the way of incentives to encourage the construction of this pipeline. I think it is very much in our national interest that it be constructed.

Senator Gramm. Mr. Chairman, could I make one point?

The Chairman. Yes.

Senator Gramm. We built the Alaskan oil pipeline without setting a floor on oil. It happened. It happened over incredible obstacles, where government made it very hard to do. But it finally happened because it was economic. We cannot do this in Alaska and not do it in the Gulf of Mexico, and not do it everywhere else.

So the question is, do we want to set a floor on the price of natural gas that is difficult, expensive, and risky to produce? I just do not think it is a good national policy.

The Chairman. I would hope that the Senator would actually withdraw his amendment. I frankly do not think it is ripe. It is not fully understood. We have no idea what the score is. It could be multi-billions of dollars.

I do not know if we have ever set a floor before, a guaranteed federal price floor. I think that has got to be examined much more closely than we have thus far. There are questions about who is going to own the pipeline, questions about other pipeline owners, questions about other energy suppliers. Are we going to give them the same treatment or not? I doubt that we are. I understand the need for more gas, but I don't think this is the right amendment to address that problem.

I would urge the Senator to withdraw his amendment, but if he is not going to withdraw it and he wants a vote, I would urge us, regrettably, not to accept this amendment, not to vote for this amendment. There are just too many questions.

Senator Murkowski. Well, Mr. Chairman, there are a lot of questions that are not answered around here. One of them was what we started in on with the first discussion and the exposure that the committee has relative to the Chairman and the Ranking Member getting back to us.

So, while I respectfully recognize your point, I do not accept it. I do not think that you are talking about, here, a matter of similar treatment. I think the Senator from Texas mischaracterizes it, because clearly the activities in deep water enjoy deep-water royalty relief, and they should. Otherwise, they would not be developed out there because the risk is simply too great and the cost is too high.

Another thing that characterizes the issue that I think is significant. That is, you have got your infrastructure already in. We do not have the infrastructure in. The infrastructure is the pipeline.

This would be the largest construction project in the history of North America: $20 billion to take this gas down.

Now, it is not my fault that they have not scored it. We have asked and presented it. I think it is very difficult to score because the way it is presented is presented with a payback.

Now, that means that the government, over the term of the pipeline, would receive--and there would be obviously some conditions on what that would be--back whatever it basically had to offset in any given year, depending on the price of gas.

Now, that is different than what you had before. I grant you, it requires some evaluation. But to suggest somehow that this is the same as we have done before, it is not. It is not necessarily setting--

Senator Nickles. Would the Senator yield for a question?

Senator Murkowski. Yes. Go ahead.

Senator Nickles. The payback begins when the price--let us say that a lot of money has been paid, but if the price goes above $3.75, then payments are made?

Senator Murkowski. Yes. We are talking about the projections on the price of gas.

Senator Nickles. All right.

Senator Murkowski. What was gas here three months ago, four months ago? Seven dollars, something like that.

Senator Nickles. At Henry's Hub?

Senator Murkowski. Yes.

Senator Nickles. Henry's Pub.

Senator Murkowski. Henry's Pub.

The Chairman. All right.

Senator Murkowski. We have got to recognize that this is a projection to try and bring a project along that you are not going to bring along unless--and this is a lead-time project. It is going to take a long time to bring this along. Unless there is an incentive in here, it is not going to happen.

The Chairman. Senator Kerry?

Senator Kerry. Mr. Chairman, I wonder if it makes sense, if the Senator from Alaska might be willing, to not vote on this one today. Some of us are disposed to, I think, want to try to be thoughtful about it.

But I think that, given the lack of scoring and some of the other questions raised, maybe it makes sense not to vote on it now and see if we can work on it. I think it only got presented to us, what, yesterday. Am I correct? Yes. So I think if we could spend a little time on it, it might be more advantageous.

The Chairman. That would be my preference, too, if I might ask the Senator.

Senator Grassley. You are really saying between now and the time the bill comes up on the floor of the Senate, work on it now.

The Chairman. Right. To the best we can.

Senator Murkowski. Well, with the assurance of the Chairman and the Ranking Member that we can get something on this that is realistic, I will withdraw the amendment. But several of us are going to be down on the floor on this, and I would like to reserve the opportunity.

Since we are already, perhaps, going to have one other opportunity here later with whatever the Chairman and the Ranking Member get back to us with, to at least have the opportunity to discuss this. You should have a scoring at that time.

Ms. Paull. We will work diligently. The materials you submitted were submitted near the end of January, and we have really been working hard to get the mark put together for this mark-up. So, we will turn our attention to it.

Senator Lott. Mr. Chairman, I do not want to prolong this, but if I could just say one word. Senator Murkowski is doing the right thing at this point. I respect so much his leadership in the energy area and what Alaska has done to try to help us with our energy needs.

I do not think, in all my years in Congress, I have ever voted against an Alaskan amendment, particularly one by Senator Murkowski, and I do not want to begin now. I am not inferring that I will.

But I was not aware of this. I think to have a little more time to know what the scoring is and have a chance to look at it further and discuss it with Senator Murkowski would be helpful for all of us.

The Chairman. I might say to the Senator, too, I very much understand what he is trying to do. I think it is the right objective, and do want to work with you, Senator, to work out a solution here.

Senator Murkowski. I will withdraw the amendment. But I would also like to know, in the mark, is there not still a $10 billion guarantee that is in the existing bill? That is not your jurisdiction.

Senator Nickles. It is in your jurisdiction. It is in Energy's jurisdiction.

Senator Murkowski. Well, I understand. But let us be realistic. There is a $10 billion guarantee proposed in the underlying energy bill.

Senator Bingaman. There is a guarantee for 80 percent of the cost of any construction within the U.S., down to the Canadian line.

Senator Murkowski. That is six months afterwards. My contention here, is that does not provide what is needed here for this project. It is a good effort, but it is just not enough.

Now, when you the Senator from Texas looks at a guarantee, I assume he has got a little different perspective.

Senator Gramm. Well, my response is, if you cannot do it with an 80 percent loan guarantee, it ought not to be done.

Senator Murkowski. Well, I do not think you would support an 80 percent loan guarantee.

Senator Gramm. No, I would not. Of course not.

The Chairman. We are going to have this debate, I think, in many other forums.

I would like to offer an amendment, on behalf of Senator Kyl, who had to leave. This amendment directs the GAO to undertake an ongoing analysis of the effectiveness of alternative vehicles and fuel incentives, and conservation and energy-efficient provisions contained in the mark. That is essentially the amendment. Without objection, the amendment is agreed to.

Senator Hatch. Mr. Chairman? Wait a minute, Mr.

Chairman. He does not take into consideration the environmental benefits. Could we add that?

The Chairman. Well, he is not here. Do you want to amend it?

Senator Gramm. What do you want to do on it?

Senator Hatch. Well, I think you ought to take into consideration the environmental benefits and cost savings there as well. He does not take that into consideration.

Senator Gramm. What is his amendment?

Senator Hatch. He has the GAO investigation or report on the Clear Act. We ought to at least include the environmental considerations as well, because that is part of it.

The Chairman. Well, I think that is a good idea, but that is not his amendment.

Senator Hatch. Well, we will do it on the floor, maybe.

Senator Murkowski. Mr. Chairman?

The Chairman. Senator Murkowski?

Senator Murkowski. I need a clarification on Section 45 of the Electricity Production Credits. There is language in here that states that eligible forest-related resources would be defined as--

The Chairman. Senator, if you will, I have been informed that we have not disposed of the Kyl amendment.

I thought that I said "without objection it is agreed to," and I will say it again. Without objection, the Kyl amendment is agreed to. All right.

Senator Murkowski?

Senator Murkowski. [Continuing]. "Mill residue/brush, but not including any old growth. Now, that precludes all of the standing timber in my State. We have virtually nothing other than old growth. Thirty percent of the old growth is dead or dying.

We would be precluded from participating in any of this biomass effort if, indeed, the interpretation of old growth is as proposed. What is old growth? Is there a definition of that? There is no agreed-to definition of old growth, to my mind. What is a dead tree or tree that is in the process of dying? What this is, is the biomass subsidy.

Ms. Paull. Senator, there is no definition in the statute. I personally do not know the origin of this.

Senator Murkowski. You have got three new qualifying energy sources here. You have go open-loop biomass, which is a program I think we should support. The current proposal defines biomass as "any solid, non-hazardous, cellulose waste material," et cetera, et cetera, et cetera. Eligible forest-related resources would be defined as mill residue/brush, but not including any old growth.

Now, if you are going to get the mill residue, you have to cut something down. Otherwise, you are not going to have the wood fiber. If it comes from old growth, we have never--

Senator Lott. Well, the question is, Frank, that you are asking, I guess, is why do we have that exception?

Senator Murkowski. I would like to either be exempted from it and you can leave the exception in, or broaden it to say timber resources that can really be used for wood fiber, for practical purposes, or waste wood.

The Chairman. Well, let us get the facts here, first.

Senator Murkowski. All right.

The Chairman. Ms. Paris, could you explain this provision?

Ms. Paris. I do apologize. We do not have a definition that is within this particular provision. But it is my understanding that the old growth timber exclusion was in there to preclude the use of those trees that otherwise being used for board use, things to that effect. They are not to be burned.

Senator Murkowski. You cannot afford to take quality old growth and burn it up in biomass. It has got a value much higher in lumber.

Senator Lott. Yes. But the residue that you have.

Senator Murkowski. Yes. They say you cannot use that either.

Senator Lott. Well, you ought to be able to use it.

Senator Gramm. Well, either you want to do this stuff or you do not.

The Chairman. Well, this is a question. Let us add this to your list, Senator, of things we are going to work out between now and the floor.

Senator Murkowski. Well, you are from a timber State. You know.

The Chairman. I know. But there was no definition here and we have got to work it out.

Senator Lott. I would hope that we would look at what that definition should be, or in the alternative, just cut out that phrase that excludes old growth. That is a simple solution. But, at any rate, some explanation.

Senator Gramm. Mr. Chairman?

Senator Murkowski. What is old? At what point does growth get old?

The Chairman. Is there further discussion? Senator Gramm?

Senator Murkowski. I would like to be included in this somehow. So if I have got your commitment that we will try and address this through a definition--

The Chairman. We will work on it.

Senator Gramm. Mr. Chairman, a motion to strike is always in order, right?

The Chairman. Yes. Before you get to that, apparently Senator Kyl agrees to modify the amendment, as suggested by Senator Hatch. So, without objection--

Senator Nickles. Mr. Chairman, could I make a further modification to the Kyl amendment?

The Chairman. Well, I had better check with Senator Kyl's staff, because he is not here.

Senator Nickles. Well, we modified it to include the environmental benefits, as requested by Senator Hatch, and I think that is fine. I think we also should request GAO to report back to Congress who benefits from these various provisions.

Senator Lincoln. Mr. Chairman, I misunderstood. I thought you did not accept the environment.

Senator Nickles. We did.

The Chairman. Wait a minute. We did.

Senator Lincoln. Oh, you did?

The Chairman. It was added in. It was a suggestion by Senator Hatch to the underlying Kyl amendment.

Senator Nickles. And Senator Kyl's staff informed us they have no objection.

The Chairman. To?

Senator Nickles. To also ask GAO to report back to us who benefits from the various provisions we are passing.

The Chairman. All right. As modified, without objection, the amendment is agreed to. All right.

If there are no further amendments--

Senator Gramm. Mr. Chairman, we have a requirement in here that we hit a 20 percent renewable energy component in electric power generation. I had intended to move to strike that provision. It seems to me, in lieu of striking it, I would like to propose that we strike the 20 percent and insert 10 percent. I do not need a long debate, everybody understands it.

Basically, that is a very huge requirement we are imposing on electric utilities. Some of them will have a very difficult time meeting it. It could drive up utility costs very substantially, especially in rural areas. I think 10 percent is more reasonable than 20.

The Chairman. Senator, I might add, which amendment it is you are referring to, as you well know, under the committee rules, amendments have to be filed by 5:00 prior. So are you talking about the energy bill or are you talking about our bill?

Senator Gramm. The underlying tax provision. This is the requirement in the electric restructuring. One of the provisions is that there is a 20 percent requirement.

Senator Bingaman. If you are referring to the energy bill itself--

Senator Gramm. That provision is not in this bill.

Senator Bingaman. We have renewable portfolio in there. It is not 20 percent, it is 10 percent.

Senator Grassley. Mr. Chairman?

The Chairman. Senator Grassley?

Senator Grassley. I move that the committee adopt the Chairman's mark, as amended, and report the bill favorably.

The Chairman. All those in favor, say aye.

[A chorus of ayes]

The Chairman. Opposed, no?

[No response]

The Chairman. We had a motion, it was agreed to, and it passes.

Senator Grassley. I would ask that the staff have the authority to draft necessary technical and conforming changes to the bill.

The Chairman. You have got it.

Senator Thompson. Mr. Chairman? I understand there is a technical problem with the geothermal heat pump provision contained in your modification. I would just like to get your assurance we can work together to resolve this between now and the Senate floor.

The Chairman. You have got it.

Senator Thompson. Thank you.

The Chairman. You have got assurance.

There is no further business before the committee. The meeting is adjourned.

[The prepared statement of Senator Kyl appears in the appendix.]

[Whereupon, at 6:59 p.m., the meeting was concluded.]

A

I N D E X

UNITED STATES SENATE
COMMITTEE ON FINANCE
Max Baucus, Chairman

Wednesday, February 13, 2001
4:00 p.m.
215 Dirksen Senate Office Building

Agenda for Business Meeting

I. To mark up an original bill establishing Energy Tax Incentives

STATEMENT OF SENATOR KERRY
FINANCE COMMITTEE EXECUTIVE SESSION
FEBRUARY 13, 2002

ENERGY EFFICIENT APPLIANCES

I want to thank the Chairman and Ranking Member for including a provision I requested to provide consumer credits for the purchase of highly efficient appliances for residential use in the Energy Tax Incentives Act of 2002. This includes air conditioners, heat pumps and water heaters and other appliances. The proposal is estimated to cost $433 million. I also want to thank Senator Bingaman, who cosponsored the amendment.

Electricity demand is growing nationally. This increased demand should be met through a combination of new generating capacity and efficiency. This proposal, coupled with other parts of the Act, helps strike that balance. It will also save consumers money and cut pollution, while providing consumers the comfort and amenities they desire.

Importantly, the proposal will also enhance reliability in the electric system. It does this by including an energy efficiency ratio (EER) rating for air conditioners and heat pumps. These standards target peak demand situations in the electricity system and bolster overall system reliability. For example, during hot weather electricity demand peaks because of increased use of air conditioning equipment, and system reliability can be compromised. The EER rating for air conditioning equipment targets high temperature operation. By capturing efficiency gains under these high temperature scenarios, the measure targets those peak demand days when the overall electric system is most vulnerable and electricity prices are likely higher.

Finally, earlier versions of this proposal were endorsed by Trane, Carrier, and Goodman, who together make 60 percent of all air conditioners. I'm pleased the proposal has that kind of broad industry support.

Again, I thank the Chairman and our Ranking Member for accommodating this important proposal.

Opening Statement of Senator Orrin G. Hatch
before the
Committee on Finance
Markup of Energy Tax Provisions
February 13, 2002

Thank you Mr. Chairman. I applaud you for holding this markup today. You and Senator Grassley deserve credit for putting forth an energy incentive tax package that is both broad in scope and bipartisan in nature. I am particularly pleased that your mark incorporates the CLEAR ACT, the most comprehensive legislation Congress has yet considered to promote the use of alternative fuel vehicles and advanced car technologies. Both of you and your staffs have been very helpful in finding a way to include this proposal in the Chairman's mark.

Transportation accounts for about two-thirds of the oil consumption in the United States, and we are 97 percent dependent on oil for our transportation needs. When we consider the role transportation plays in our economy and our way of life, it is hard to believe that we rely on foreign sources for more than one-half of our oil supply. If our nation is going to have a strategy for energy security, that strategy must begin with transportation fuels.

Advances in alternative fuels and new vehicle technologies have been significant in recent years. However, three basic obstacles stand in the way of a broad shift toward their adoption. These are the higher cost of the vehicles, the higher cost of alternative fuels, and the lack of an infrastructure of alternative fueling stations.

For more than three years now, Senators Rockefeller, Jeffords, and I have worked together to come up with a well-constructed and comprehensive answer to these market barriers. This year, with the additional help of Senators Kerry and Snowe, among others, we introduced the CLEAR ACT, which stands for Clean Efficient Automobiles Resulting from Advanced Car Technologies.

The CLEAR ACT would lower the barriers that stand in the way of widespread consumer acceptance of these advanced technology and alternative fuel vehicles by providing tax credits to consumers who purchase hybrid electric, fuel cell, battery electric, and dedicated alternative fuel vehicles. It would also would provide incentives for the purchase of alternative fuels and the development of an alternative fuel infrastructure.

Without imposing any new mandates, the CLEAR ACT focuses on the very best emerging technologies to help our citizens to enjoy the health benefits of cleaner air sooner, to help our communities to enjoy the economic benefits of attaining clean air standards sooner, and to help us reduce our consumption of foreign oil sooner than would otherwise be possible.

Not long ago, a well-intentioned program to promote alternative fuel vehicles by the Arizona legislature experienced extreme cost overruns and failed to provide the promised energy and environmental benefits. I want to assure the members of this committee that we have studied the Arizona experience, we have identified the inherent weaknesses of that model, and we have been careful to avoid each one of them.

With the CLEAR ACT, until a new advanced vehicle is purchased, until new infrastructure has been installed, or until alternative fuel is placed in the tank of a dedicated alternative fuel vehicle, there will be no cost to the Treasury. And when a cost is incurred, it will be a small cost relative to the resulting environmental benefits and energy savings.

Again, I thank the Chair and Senator Grassley for their leadership on this issue, and I look forward addressing the energy tax incentives before the committee this afternoon.

Statement of Senator Olympia J. Snowe for the

Finance Committee Markup for Energy Tax Credit Incentives
February 13, 2002

Mr. Chairman, we are here today to develop responsible tax credit incentive policies that will increase the efficiencies of the electricity we produce, the vehicles we drive, the appliances we use, the homes in which we live, and, in turn, enhance the competitiveness of our domestic manufacturers. This is why I am pleased to note numerous tax incentives in the Mark – and others that are now included in the Chairman's Modification – that I have sponsored or cosponsored through a variety of bills.

The entire world - particularly the developing and fast-growing nations of China, India, and Brazil - desperately needs access to clean, low cost, energy-efficient and renewable resources. The key is to make the best renewable and alternate energy systems competitive with today's non-renewable sources of energy so that they can be developed and used both at home and sold abroad.

At the same time, since you held the first energy tax credit incentives hearing last July, Mr. Chairman, the entire nation has been going through a fundamental reassessment of its energy infrastructure since the horrific events of September 11. We realize now more than ever that we must reduce our vulnerabilities to terrorism with more secure and reliable distributed energy delivery systems rather than solely relying on our current centralized infrastructure of pipelines, refineries, power plants, electricity grids and oil tankers berthed in our harbors. And, the United States simply cannot continue to spend $57 billion a year buying oil from the Middle East.

Mark Twain once wrote that "few things are harder to put up with than a good example", but in this instance we can be grateful to have some excellent examples to turn to. Sweden, for instance, gets 19 percent of its electrical energy using forestry and farm biomass. I am pleased to be a cosponsor of the GREEN Act that is included in the Mark that will give tax credits for producing electricity from biomass such as forest and cellulosic wastes.

Another example is Denmark who, in the last 15 years, has developed energy from wind that supplies 18 percent of its electric needs. Here in the United States, 20 percent of our power comes from nuclear power plants, which are clearly more obvious and dangerous targets for terrorists. This is why I am a cosponsor of the BREEZE Act to stimulate more energy from wind power in the U.S., which is also in the Mark.

We need to expand the mix of the country's energy sources with the realization that power from nuclear and fossil fuels will continue to be large part of the energy basket in the next decades - but we must encourage safer, cleaner and decentralized sources as well. The fossil fuel industry itself is very good at reading the tea leaves as British Petroleum is the world's largest producer of solar cells. Another bill I cosponsored expands the credit for electricity from sources such as solar, and also geothermal, and landfill gas. This particular Reid bill also allows tradable tax credits for renewable energy sources that would help municipal electric utilities, public power utilities, and rural cooperatives build more electricity facilities.

Our task is to help make it more attractive, through the tax code, for our U.S. manufacturers to get the most promising and cost-effective technologies to the U.S. and global marketplace with all due speed. The CLEAR Act, for instance, for which I am a cosponsor, promotes the purchase of clean hybrid vehicles that are powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells and other clean sources that will benefit the air we breath. We should also help to increase the American public's awareness of the benefits to our health and our national security of encouraging the shift away from foreign fossil fuel and toward domestic renewable and alternative energy sources and manufacturing technologies.

We have financial constraints as the Chairs of the Committee have given us the mark of approximately $14.5 billion with which to work, so we must do our best to make the wisest tax incentive choices for U.S. consumers and manufacturers that will get us the biggest and fastest possible energy efficient and economic benefits.

Ironically, we have had the knowledge of these alternative and renewable sources for over a century as the simple principle of fuel cells - combining hydrogen and oxygen to produce electricity and pure water - and the photovoltaic principle behind the solar power of the sun, which were both discovered or discussed in 1839 - 163 years ago. I am pleased that the Chairman's Modification that has been put before us today has included the incentives for solar energy facilities in the Section 45 electricity production credit. We should ask ourselves why, instead of our daily diet of approximately 19 million barrels of oil a day, we weren't also choosing to bolster development of these sources of energy for our consumption and to grow our economy.

Imagine automobiles driven by fuel cells - our U. S. auto manufacturers and the government are already investing in fuel cells. Imagine businesses and homes having their own free-standing and reliable fuel cells - one of the cleanest means of generating electricity - as is promoted in the Chairman's Mark with tax provisions from the Lieberman/Snowe fuel cell legislation. Fuel cells can provide electricity instead of our current vast, centralized fossil fuel systems that make our air dirtier and less healthy, causing us to spend millions more on health care dollars each year.

I am pleased to see provisions of my bill, S. 1873, included in the Mark that gives tax incentives to build more energy efficient new homes and to have included in the Modification the consumer tax credit that encourages consumers to install in their existing homes certifiable high energy efficient superwindows, such a low emissivity glass. Many American homes were built years before energy efficient technologies were even developed and windows are responsible for a great deal of energy loss through seepage. Since homeowners continuously make improvements to their existing homes by making additions and installing new windows and doors, encouraging more efficient windows and doors will decrease our energy consumption and save taxpayers money through their energy bills. And, because energy usage is reduced by the installation of superwindows, emissions of carbon dioxide -- the major greenhouse gas related to climate change -- are also reduced. I also am a cosponsor of S. 207, and its provision for promoting greater energy efficiency in commercial buildings has been included in the Mark as well. We can find huge energy savings in this sector.

We need to encourage through incentives the purchase of better energy efficiency in the appliances we use in our homes, and I am very pleased to see the Chairman's Modification includes a personal tax credit for energy efficient electric heat pump hot water heaters. In my State of Maine, for instance, we have a company, the Nyle Company in Bangor, that makes this product, the installation of which is easy, low cost and requires no change in lifestyle. These heat pump heaters can reduce electric usage for hot water heating by more than 50 percent. These heaters can extract heat and humidity from the surrounding area, reducing the need for dehumidifiers and reducing air conditioning loads, which saves even more energy. Even a small percentage of the market represents a huge reduction in demand and usage and will greatly jumpstart this market.

The bottom line is, we have the opportunity to raise the bar for our future domestic energy systems. Solutions exist in available and developing technologies, and most of all in the entrepreneurial spirit of the American people. As Theodore Roosevelt once said, "Conservation is a great moral issue, for it involves the patriotic duty of ensuring the safety and continuance of the nation." I couldn't agree more and I thank the Chairman Baucus and Ranking member Grassley and their staffs for their assistance in including in the Mark and the Modification provisions that I strongly support.

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STATEMENT OF SENATOR JON KYL FOR THE RECORD OF THE MARKUP ON THE ENERGY TAX INCENTIVES ACT OF 2002 COMMITTEE ON FINANCE U.S. SENATE

I am pleased to have this opportunity to consider the important proposals we have before us in the Finance Committee relating to energy policy and more specifically, electricity tax issues. I thank the Chairman and the Ranking Member for giving the Finance Committee the opportunity to make its recommendations to the full Senate on energy tax proposals, particularly in electricity.

As a member of the Finance and Energy Committees, I have the benefit of seeing first-hand the inconsistent approaches taken in Federal energy and tax laws as they relate to the electricity industry. A glaring example of one of those inconsistent approaches is in the Energy Policy Act of 1992 and the private use rules of the Internal Revenue Code, which pre-date the Energy Policy Act and applicable, as you know, to public power utilities. While our Federal energy policy since 1992 has been to open electric markets to wholesale and even retail competition, our tax code contains restrictions dating back to the Tax Reform Act of 1986 that make it difficult and in some cases impossible for publicly-owned utilities to comply with that policy.

In an attempt to remove the tax code impediments to participation in the newly restructured electric industry, the publicly-owned and privately-owned utilities labored for several years to develop a package of tax law changes that would not change the competitive balance between the two sectors, yet would provide the necessary flexibility to comply with the new energy policy provisions being implemented by the Federal and state governments.

The fruit of those efforts was S. 972, introduced last year by Senators Murkowski, Thompson, Breaux and Jeffords. I joined as a cosponsor of this bill. In the House, H.R. 1459 was introduced by Congressman J.D. Hayworth and was co-sponsored by 16 other members of the Ways and Means Committee. These bills represented a landmark effort to accommodate some divergent views of public power and investor-owned utilities on a range of federal tax issues.

The private use provisions in S. 972 represent years of negotiations between the respective sectors of the industry and reflect a delicate, equitable balancing of interests. Importantly, the bill grandfathers existing bonds from private use restrictions if the issuing municipal or state utility elected to terminate permanently its ability to issue tax-exempt debt to build new generation facilities.

The House companion bill, however, was negatively altered during passage. The bill as approved by the Ways and Means Committee bill (H.R. 2511,The Energy Policy Act of 2001 and subsequently in the House-passed H.R. 4 (Securing America's Future Energy Act of 2001) contains material modifications to the original bill. In fact, certain modifications are even more restrictive than existing law and temporary IRS regulations and work absolutely counter to national energy policy and the efficient operation of our country's electric infrastructure. Indeed, the various conditions set forth in the bill will discourage utilities from taking the necessary steps to advance open access. Examples of the most problematic provisions are:

- Eliminating the ability of municipal utilities that elect to forego issuance of future tax-exempt bonds for generation from refunding outstanding tax-exempt generation bonds, even though this can result in savings to the utilities' customers and the U.S. Treasury. The bill can also prohibit these electing utilities from tax-exempt financing limited repairs and environmental improvements, including those which may be government-mandated.

- In the context of sales of energy, provisions that restrict or eliminate the ability to use long-standing statutory and regulatory exceptions to the private use rules and provisions that impose significant new constraints on new rules that were designed to enable public power to participate in a deregulated environment. As an example, language in the bill effectively precludes sales to rural electric cooperatives that were one of the exceptions to the private use rules. The bill appears to provide that the expansion of an existing generation facility ca result in loss of eligibility of the entire facility for permitted exception treatment for long-term take or pay requirements contracts, even if the cost of the expansion was financed with taxable debt or equity. Further, for a public power that entity owns no transmission, it will qualify for the bill's clarifications to the private use rules only if <u>all</u> transmission providers who provide transmission to that municipal utility's customers provide open access on <u>all</u> of their transmission facilities. These types of restrictions reduce or eliminate many of the benefits intended in the bill.

- New restrictions on tax exempt bonds for transmission facilities that will prevent municipal utilities from using tax-exempt bonds to finance new transmission facilities to connect new power plants to their service areas. In addition, new restrictions in the bill require that, to qualify for private use relief, public power transmission facilities must be owned, directly connected to customers and necessary to serve those customers. Thus, the bill ignores the need for investment in new transmission for maintenance of grid reliability, the multiple legal forms of ownership and use of transmission (including the different forms of RTOs and related organizations, leasehold and operational arrangements) and the fundamental physics involved in transmission network operation.

- The revision of the new exception to the private use rules for sales of certain lost load to require <u>proof</u> that the load loss was "attributable to open access" in order to utilize this exception, which was designed to ensure that our nation's energy capacity is fully utilized.

I had hoped that these problems could have been resolved by my colleagues on the Finance Committee and myself, but the revenue constraints imposed on us have prevented us from rectifying these problems. The Committee staff has been most helpful in trying to understand public power's situation, and I welcome their efforts. Much attention has been focused on some kind of relief for already–issued bonds. While appreciative of the intent, public power has been reluctant to agree to these offers for several reasons:

(1) the proffered relief appeared to mirror some of the provisions pertaining to existing bonds in the temporary regulations, relief which currently does not require a revenue score; and

(2) the proffered relief was not able to be reduced to writing, and therefore, it was unclear whether it was better, worse, or essentially equivalent to the temporary regulations.

In these discussions, public power suggested a couple of smaller provisions to ameliorate the current private use problem, not as a substitute for S. 972, but just as interim flexibility for publicly-owned utilities in the still-changing marketplace. Unfortunately, there apparently has not been enough time for staff to review these suggestions adequately. I am hopeful, however, that public power may be able to come up with some useful provisions prior to this bill going to conference. Accordingly, I would like to continue to work with the Chairman and Ranking Member as we go forward. Certainly, we would not want this bill, because of its relief for IOUs and coops, to shift the competitive balance in the marketplace.

I want the Chairman and Ranking Member to know that I remain committed to solving the problems that the electric industry faces in the evolution of the marketplace. If this is not the appropriate vehicle due to revenue constraints, I will continue to search for another. These legal obstacles require removal, sooner rather than later.

Statement for Finance Committee
Hearing on Canadian Softwood Lumber
Senator Larry E. Craig
February 13, 2002

Mr. Chairman and Mr. Grassley, thank you for this opportunity to speak in front of the Committee regarding the Canadian softwood lumber dispute on behalf of my state of Idaho. The Canadian softwood lumber issue continues to threaten the very core of the timber industry in my state and numerous other states. Without resolution, our timber industry will continue to suffocate at the expense of unfairly traded Canadian lumber.

This issue has devastated us for nearly two decades. During this time, we have been able to agree on quick fixes that provide short term relief for our lumber companies. Once again, however, we are at a crossroad, with the latest trade agreement between Canada and the United States expiring nearly a year ago. Since the expiration we have seen roughly a 10 percent increase of Canadian lumber in our markets. This surge has caused our mills to close and continues to force those remaining mills to cut jobs as they find ways to survive in this troublesome market.

Our U.S. timber industries are impacted by the differences in the Canadian and U.S. market. While Canada is allowed to trade in U.S. markets, our timber companies are not allowed to trade in Canadian markets. Let me say that again, U.S. timber companies are not allowed to trade in Canadian markets. Not only is the Canadian government having a profound effect on our timber industry, but our government has tied the hands of our fellow citizens by continuing this ridiculous trade policy. I support free trade; however, this situation does not even fall in the gray area of free trade. This issue is black and white: when one market is not open nor supportive, of outside companies entering the market, it is not free trade and would certainly not qualify as fair trade.

The importation of softwood lumber is the straw that is braking the camel's back of our timber industry. Our companies already struggle with many issues, including access to public lands, rising energy prices, and production costs. However, when Canadian companies have an upper hand with reduced production costs and are allowed to flood our market with their product, our companies can hardly compete. The contract agreements between the Canadian Government and timber companies provide for a subsidy that results in a mandate to harvest, regardless of the market needs. Any new agreement needs to address this issue by promoting a fair trade environment that stabilizes the differences between the two industries. If not, our trade laws must be vigorously enforced.

I firmly support the filings of the Coalition for Fair Lumber Imports with the International Trade Commission (ITC) and Department of Commerce. In its preliminary rulings, the ITC has determined there is a reasonable indication that our timber industry is threatened with material injury as a result of softwood lumber imports from Canada that are subsidized and dumped in our markets at a 32 percent unfair advantage. The ITC will hold a hearing on this issue in March and make its final decision in May. Along with my colleagues, we are urging the Department of Commerce and ITC to apply the strictest letter of the law in this case and provide our U.S. timber industry with relief from the unfairly traded Canadian lumber. With this verdict, I am hopeful that the United States and Canadian Governments will then be able develop a long term solution to a problem that continues to plague our U.S. timber industry.

BACKGROUND INFORMATION RELATING TO THE INVESTMENT OF RETIREMENT PLAN ASSETS IN EMPLOYER STOCK

Prepared by
the Staff of the
JOINT COMMITTEE ON TAXATION

February 11, 2002
JCX-1-02

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INTRODUCTION

Recent events have focused public attention on issues related to the investment of qualified retirement plan assets in employer stock, including the potential effect on retirement security and the need for plan participants to understand sound investment practices. This document,[1] prepared by the staff of the Joint Committee on Taxation, provides background material relating to these issues.

This document contains the answers to frequently asked questions related to qualified retirement plans and the investment of plan assets in employer stock, data on the most common types of qualified retirement plans, and a summary of current legislative proposals.

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[1] This document may be cited as follows: Joint Committee on Taxation, *Background Information Relating to the Investment of Retirement Plan Assets in Employer Stock* (JCX-1-02), February 11, 2002.

I. QUESTIONS AND ANSWERS RELATING TO EMPLOYER-SPONSORED RETIREMENT PLANS

A. General Questions and Answers Relating to Employer-Sponsored Retirement Plans

1. Is an employer required to offer retirement plan coverage to its employees?

No, an employer is not required to offer retirement plan coverage to its employees. The employer generally decides whether to offer a retirement plan to its employees and, if it does, has the ability to set many plan terms, including the level of benefits. In the case of employees covered by a collective bargaining agreement, retirement benefits are subject to the bargaining process. Thus, the retirement plans and benefits available to employees vary from employer to employer.

2. What types of retirement plan arrangements are available to employees?

There are two broad types of retirement arrangements that an employer may provide: qualified retirement plans and nonqualified deferred compensation plans or arrangements. A qualified retirement plan is a plan that meets requirements set forth in the Internal Revenue Code of 1986 (the "Internal Revenue Code") (see Q&A A.3., below). Qualified plans are also subject to regulation under the Employee Retirement Income Security Act of 1974 ("ERISA"). In contrast to qualified plans, nonqualified plans are subject to relatively few restrictions under the Internal Revenue Code. In addition, if a nonqualified plan is limited to a select group of management or highly compensated employees, it is generally not subject to ERISA. Under ERISA, such a plan is referred to as a "top-hat" plan.

3. What is a qualified retirement plan?

A qualified retirement plan is a plan that meets requirements set forth in the Internal Revenue Code. In order to provide an incentive to employers to offer qualified plans, the Internal Revenue Code provides favorable tax treatment to such plans. If the Internal Revenue Code's qualification requirements are satisfied, the employer is entitled to a current deduction for plan contributions (within limits) and employees are not taxed on plan benefits until received.

There are two general types of qualified retirement plans, defined contribution plans and defined benefit plans.

4. What is a defined contribution plan (or individual account plan)?

A defined contribution plan is an employer-sponsored retirement plan that provides an individual account for each participant. The participant's benefits are based solely on the participant's account balance, which consists of contributions to the account and adjustments to reflect earnings and losses. Depending on the design of the plan, contributions may consist of pre-tax or after-tax employee contributions, employer matching contributions (i.e., employer contributions that are made only if an employee makes contributions to a plan), and other employer contributions. Under ERISA, a defined contribution plan is also referred to as an individual account plan.

Particular types of defined contribution plans include profit-sharing plans, stock bonus plans, employee stock ownership plans ("ESOPs") (see Q&A A.9., below), 401(k) plans (see Q&A A.10., below), and money purchase pension plans. The legal requirements applicable to each type of plan differ somewhat.

5. What is a defined benefit plan?

A defined benefit plan specifies a formula under which a participant's retirement benefits are determined, usually based on compensation and years of service. The plan does not maintain individual participant accounts or earmark plan assets for particular participants. Employer contributions to a defined benefit plan are subject to minimum funding requirements to ensure that plan assets are sufficient to pay the benefits under the plan. Defined benefit plan benefits are insured by the Pension Benefit Guaranty Corporation (see Q&A B.6., below).

6. What is a hybrid plan?

A hybrid plan is a plan that has features of both a defined benefit plan and a defined contribution plan. For example, a cash balance plan is a hybrid plan. Technically, a cash balance plan is a defined benefit plan; however, plan benefits are defined by reference to a hypothetical account balance.

7. What laws govern employer-sponsored retirement plans?

The Internal Revenue Code and ERISA both regulate qualified retirement plans. Nonqualified retirement plans or deferred compensation arrangements are not subject to the Internal Revenue Code's qualification requirements. In addition, if such plans are available only to a select group of management or highly compensated employees, they are also not subject to ERISA.

Some of the provisions of the Internal Revenue Code and ERISA applicable to qualified retirement plans are identical or very similar. For example, both the Internal Revenue Code and ERISA impose minimum participation and vesting requirements.

In addition, the Internal Revenue Code contains requirements not included in ERISA, such as nondiscrimination rules that are designed to ensure that the plan governs a broad group of employees. The Internal Revenue Code also limits the amount of contributions (including employee contributions) and benefits that can be provided under a qualified plan.

Similarly, ERISA contains provisions that are not included in the Internal Revenue Code. For example, ERISA contains basic fiduciary standards that apply to retirement plan fiduciaries.

8. How are the rules relating to qualified retirement plans enforced?

The qualification requirements under the Internal Revenue Code are enforced by the IRS. If a plan fails to meet the qualification requirements, then the favorable tax treatment for such plans may be denied; that is, the employer may lose tax deductions and employees may have current income taxation. As a practical matter, the IRS rarely disqualifies a plan. Instead, the

IRS may impose sanctions short of disqualification and require the employer to correct any violation of the qualification rules.

Certain of the Internal Revenue Code rules relating to qualified plans are enforced through an excise tax rather than through disqualification. For example, a failure to satisfy the minimum funding requirements for defined benefit plans (see Q&A A.5., above) does not result in disqualification of the plan. Instead, an excise tax is imposed on the employer.

Employees do not have a right to sue to enforce the Internal Revenue Code's requirements.

ERISA's requirements generally may be enforced through administrative actions by the Department of Labor or by lawsuits brought by plan participants, the Department of Labor, or plan fiduciaries.

9. What is an ESOP?

An ESOP (i.e., an employee stock ownership plan) is a defined contribution plan that is designated as an ESOP and is designed to invest primarily in stock of the employer. An ESOP can be an entire plan or it can be only a component of a larger defined contribution plan. ESOPs are subject to additional requirements that do not apply to other plans that hold employer stock. For example, voting rights must generally be passed through to ESOP participants, employees must generally have the right to receive benefits in the form of stock, and certain ESOP participants must be given the right to diversify a portion of their plan benefits.

In addition, certain benefits are available to ESOPs that are not available to other types of qualified plans that hold employer stock. For example, an ESOP may be "leveraged," i.e., stock held in an ESOP may be purchased with loan proceeds. In a leveraged ESOP, the ESOP typically borrows from a financial institution. The loan is typically guaranteed by the employer and the employer stock is generally pledged as security for the loan. Contributions to the plan are used to repay the loan. The employer stock is held in a suspense account and released to participants' accounts as the loan is repaid.

Special tax benefits also apply to ESOPs. For example, the employer may deduct dividends paid on stock held by an ESOP if the dividends are used to repay a loan, are distributed to plan participants, or if they are reinvested in the ESOP by plan participants.

10. What is a 401(k) plan?

A 401(k) plan technically is not a separate type of plan, but is a profit-sharing or stock bonus plan that contains a "qualified cash or deferred arrangement." Under a qualified cash or deferred arrangement, plan participants may elect to contribute a part of their current compensation, on a pre-tax basis, to the plan. Such contributions are commonly referred to as "elective contributions" or "elective deferrals." A plan that contains such an arrangement is commonly referred to as a "401(k) plan" or more simply a "K plan" after section 401(k) of the Internal Revenue Code, which governs such arrangements. The Federal Thrift Savings Plan is an example of a 401(k) plan. Special rules apply to 401(k) plans, including special nondiscrimination requirements and lower limits on the amount an employee can elect to contribute.

To encourage employees to participate in a 401(k) plan, many employers provide matching contributions. For example, a plan could provide that the employer will make matching contributions equal to 50 percent of the employees' elective contributions, up to a maximum of 3 percent of compensation. Employers are not required to offer a match. Many employers provide a match because doing so makes it easier for the plan to satisfy applicable nondiscrimination rules.

In addition to or in lieu of matching contributions, some employers make "qualified nonelective contributions" for employees participating in a 401(k) plan. Like matching contributions, such contributions may make it easier for plans to satisfy the applicable nondiscrimination rules. "Qualified nonelective contributions" are contributions that are made by the employer without regard to whether the employee makes elective contributions, that are 100 percent vested, and that meet certain other requirements.

Matching contributions and qualified nonelective contributions can be made to the same plan that contains the 401(k) cash or deferred arrangement or to another plan of the employer.

B. Questions and Answers Relating to Investment of Qualified Retirement Plan Assets

1. Who makes investment decisions with respect to qualified retirement plan assets?

ERISA requires that retirement plan documents designate who is responsible for investment of plan assets. In the case of defined benefit plans, the plan trustee or other designated fiduciary makes investment decisions, unless authority to manage the investments is delegated to one or more investment managers.

In the case of individual account plans, a plan may permit participants or beneficiaries to make investment decisions with respect to their individual accounts. It is common for 401(k) plans to provide participants with investment authority with respect to their own elective contributions.

2. What is a plan fiduciary?

ERISA generally provides that a person is a plan fiduciary to the extent the fiduciary exercises any discretionary authority or control over management of the plan or exercises authority or control over management or disposition of its assets, renders investment advice for a fee or other compensation, or has any discretionary authority or responsibility in the administration of the plan.

The employer and officers or directors of the employer are only fiduciaries of a plan to the extent they meet ERISA's definition of a plan fiduciary. Such persons often are not fiduciaries with respect to a plan because they do not have authority or exercise authority with respect to fiduciary functions.

3. What is the responsibility of a plan fiduciary with respect to investment decisions made by the fiduciary?

ERISA contains general fiduciary standards that apply to all fiduciary actions, including investment decisions made by fiduciaries. ERISA requires that a plan fiduciary must discharge its duties solely in the interests of participants and beneficiaries and:

- for the exclusive purpose of providing benefits to plan participants and beneficiaries and defraying reasonable expenses of plan administration;
- with the care, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims;
- by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and
- in accordance with plan documents insofar as they are consistent with ERISA.

Certain defined contribution plans are not subject to the diversification requirement or the general prudence requirement (to the extent that it requires diversification) with respect to investments in employer stock. See Q&A C.3., below.

A plan fiduciary that breaches its fiduciary duties is personally liable under ERISA to the plan for any losses resulting from such breach.

In addition, the Internal Revenue Code provides that a qualified retirement plan must prohibit the diversion of assets for purposes other than the exclusive benefit of employees and their beneficiaries (the "exclusive benefit rule"). Plan investment decisions made by plan fiduciaries may in some cases violate the exclusive benefit rule; however, not all fiduciary violations relating to plan investments are violations of the exclusive benefit rule.

4. Who is responsible for investment decisions made by plan participants?

Under a safe harbor rule, ERISA fiduciary liability does not apply to investment decisions made by plan participants if plan participants control the investment of their individual accounts. Many employers design plans to meet the safe harbor in order to minimize fiduciary responsibilities. If the safe harbor applies, a plan fiduciary may be liable for the investment alternatives made available, but not for the specific investment decisions made by participants. This includes investments in employer stock made at the direction of the participant. Failure to satisfy the safe harbor rule means that plan fiduciaries may be held liable for the investment decisions of participants. This safe harbor is commonly referred to as the "404(c) safe harbor" because it is contained in section 404(c) of ERISA.

In order for the safe harbor to apply:

- the plan must provide at least three different investment options, each of which is diversified and has materially different risk and return characteristics;
- the plan must allow participants to give investment instructions with respect to each investment option under the plan with a frequency that is appropriate in light of the reasonably expected market volatility of the investment option (the general volatility rule);
- at a minimum, participants must be allowed to give investment instructions at least every three months with respect to least three of the investment options, and those investment options must constitute a broad range of options (the three-month minimum rule);
- participants must be provided with detailed information about the investment options, information regarding fees, investment instructions and limitations, and copies of financial data and prospectuses; and
- specific requirements must be satisfied with respect to investments in employer stock to ensure that employees' buying, selling, and voting decisions are confidential and free from employer influence.

In addition, the safe harbor applies only with respect to a transaction where a participant exercises independent control in fact with respect to the assets in his or her account. Whether a participant has exercised independent control in fact with respect to a transaction depends on the facts and circumstances of the particular case. However, a participant's exercise of control is not independent in fact if:

- the participant is subjected to improper influence by a plan fiduciary or the employer with respect to the transaction;
- a plan fiduciary has concealed material nonpublic facts regarding the investment from the participant, unless the disclosure of the information by the plan fiduciary to the participant would violate other law not preempted by ERISA; or
- the participant is legally incompetent and the responsible plan fiduciary accepts the participant's instructions knowing this.

5. How often must a plan permit participants to change investment decisions?

If the ERISA 404(c) safe harbor is being relied upon, then participants must be permitted to change investment decisions in a manner consistent with that safe harbor. Unless the ERISA 404(c) safe harbor is being relied upon, there are no specific rules regarding how often a plan must permit participants to change investments.

As a practical matter, timeframes for permitting participants to change investments are determined by the plan and are often tied to the plan's administrative systems, including the frequency with which plan assets are valued. In addition, the plan will generally specify when a participant's investment directions will be executed. For example, a transfer from one investment to another may be made on the first day of the month after the month in which the participant requested the transfer.

6. Who bears the risk of investment loss in a qualified retirement plan?

In a defined benefit plan, investment risk is generally on the employer. The Internal Revenue Code and ERISA both impose minimum funding requirements on the employer with respect to defined benefit plans to help ensure that plan assets are sufficient to provide promised benefits. If the plan suffers investment losses, then the employer may be required to increase plan contributions. In addition, benefits under defined benefit plans are guaranteed (within limits) by the Pension Benefit Guaranty Corporation (the "PBGC"). In the event a plan terminates with assets insufficient to pay promised benefits, the PBGC will pay benefits up to the maximum guaranteed amount. For 2002, the maximum guaranteed benefit for an individual retiring at age 65 is $3,579.55 per month, or $42,954.60 per year.

In a defined contribution plan, the benefit the participant is entitled to is the account balance. Thus, the plan participant bears the risk of investment losses, regardless of whether investment decisions are made by the participant or a plan fiduciary. Defined contribution plans are not guaranteed by the PBGC.

7. Are there any restrictions on the type of investments that can be made with qualified retirement plan assets?

Subject to two exceptions, the Internal Revenue Code and ERISA do not contain any specific rules as to what types of investments are appropriate (or inappropriate) for retirement plan investments. Rather, ERISA's fiduciary standards govern whether investment decisions by plan fiduciaries are appropriate.

ERISA limits the amount of employer stock that can be held by certain types of plans (see Q&A C.3., below). In addition, both the Internal Revenue Code and ERISA contain prohibited transaction rules that prohibit plan fiduciaries and other persons with a close relationship to a plan from engaging in transactions with the plan. These rules are not targeted toward particular types of investments, but rather seek to prevent self-dealing transactions.

C. Questions and Answers Relating to Investment of Qualified Retirement Plan Assets in Employer Stock

1. What kinds of plans can invest in employer stock?

The assets of either a defined contribution plan or a defined benefit plan may be invested in employer stock. However, the rules relating to such investments differ for defined benefit plans and defined contribution plans.

2. What kind of employer stock can be held by a qualified retirement plan?

ERISA generally does not limit the type of employer stock that may be held by a qualified retirement plan. The Internal Revenue Code specifies the type of employer stock that may be held by an ESOP.

Under ERISA, a qualified retirement plan may hold only a "qualifying employer security." Any stock issued by the employer or an affiliate of the employer is a qualifying employer security. In the case of a defined benefit plan (and money purchase pension plans other than certain pre-ERISA plans), in order for stock to be a qualifying employer security, the plan cannot hold more than 25 percent of the aggregate amount of the issued and outstanding stock of the same class, and at least 50 percent of the aggregate amount of that stock must be held by persons independent of the issuer.

Under ERISA, qualifying employer securities also include certain publicly traded partnership interests and certain marketable obligations (i.e., a bond, debenture, note, certificate or other evidence of indebtedness).

For purposes of ESOP investments, employer stock (referred to as "employer securities" or a "qualifying employer security") is defined in the Internal Revenue Code to mean only:

(1) publicly traded common stock of the employer or a member of the same controlled group;

(2) if there is no such publicly traded common stock, common stock of the employer (or member of the same controlled group) that has both voting power and dividend rights at least as great as any other class of common stock; or

(3) noncallable preferred stock that is convertible into common stock described in (1) or (2) and that meets certain requirements. In some cases, an employer may design a class of preferred stock that meets these requirements and that is held only by the ESOP.

3. Is there any limit on the amount of employer stock that a plan can hold?

ERISA prohibits defined benefit plans (and money purchase pension plans other than pre-ERISA plans) from acquiring employer stock if, after the acquisition, more than 10 percent of the assets of the plan would be invested in employer stock.

Most defined contribution plans, such as profit-sharing plans, stock bonus plans, pre-ERISA money purchase plans, 401(k) plans and ESOPs, generally are not subject to this 10-percent limitation. Plans that are not subject to the 10-percent limitation are referred to in ERISA as "eligible individual account plans." As discussed in Q&A C.4., below, the 10-percent limitation may apply to some 401(k) plans in which participants do not have investment discretion. There is no limit on the amount that an employee can choose voluntarily to invest in employer stock in an eligible individual account plan.

4. Can employees' contributions to a section 401(k) plan be invested in employer stock without the participants' consent?

If the plan is an ESOP, then there is no limit on the amount of an employee's contributions that can be required to be invested in employer stock without the participant's consent.

If the plan is not an ESOP and the plan provides for investment in employer stock other than by participant choice, then the 10-percent limit on investment of plan assets in employer stock applies to employee contributions (and earnings) as if they were a separate plan. That is, the portion of such a plan that consists of employee elective 401(k) contributions (and earnings) is subject to the 10-percent limitation.

This restriction does not apply if: (1) the amount of 401(k) contributions required to be invested in employer stock does not exceed more than one percent of any employee's compensation; (2) the fair market value of all individual account plans maintained by the employer is no more than 10 percent of the fair market value of all retirement plans of the employer; or (3) as noted above, the plan is an ESOP.

5. Can a plan require that certain assets be invested in employer securities with no opportunity to change investments?

A plan can generally require that some or all plan contributions must be invested in employer stock, with no opportunity to change investments, and some plans do. For example, an ESOP, by its nature, is designed to invest primarily in employer stock. Many 401(k) plans provide that the employer match is invested in employer stock. Some plans do not allow participants to elect an investment option other than employer stock. Such a plan feature is sometimes referred to as a "lockdown."

In the case of an ESOP, the Internal Revenue Code imposes a diversification requirement under which an ESOP participant who is age 55 and has 10 years of plan participation must be permitted to diversify the investment of the participant's account. The participant must be given a period each year for six years in which to diversify up to 25 percent (or 50 percent in the last year) of the participant's account, reduced by the portion of the account diversified in prior years. As an alternative to providing diversified investment options in the plan, the plan can provide for the portion of the participant's account that is subject to the diversification requirement to be distributed to the participant.

This requirement does not apply to plans other than ESOPs. Thus, for example, suppose an ESOP provides that the employer will match employees' 401(k) contributions and that the match will be invested solely in employer securities. The plan may, but is not required to, provide diversification opportunities.

II. DATA RELATING TO QUALIFIED RETIREMENT PLANS

1. What percentage of the labor force participates in an employer-sponsored qualified retirement plan?

The recent U.S. Department of Labor National Compensation Survey found that in 1999, 48 percent of private sector employees participated in employer-sponsored qualified retirement plans. The survey found that, among full-time employees, participation was 56 percent. Participation rates are higher among public sector employees. The Bureau of Census's Current Population Survey found that, in 1997, 87 percent of State and local government employees and 88 percent of Federal government employees participated in an employer-sponsored retirement plan.

2. What percentage of the private labor force participates in defined contribution plans and what percentage of the labor force participates in defined benefit plans?

The National Compensation Survey found that, in 1999, among full-time employees in the private sector, 42 percent participated in an employer-sponsored defined contribution plan and 25 percent participated in an employer-sponsored defined benefit plan. Some employees participated in both.

3. Is participation in employer-sponsored qualified retirement plans roughly the same across different sectors of the economy?

No. Participation varies with firm size and industry. Figure 1 and Figure 2 below present some of the findings of the 1999 National Compensation Survey and some of the variability of employee participation in employer-sponsored qualified retirement plans by industry and firm size.

Figure 1

Percentage of Employees Participating in Employer-Sponsored Qualified Retirement Plans in Select Industries, 1999

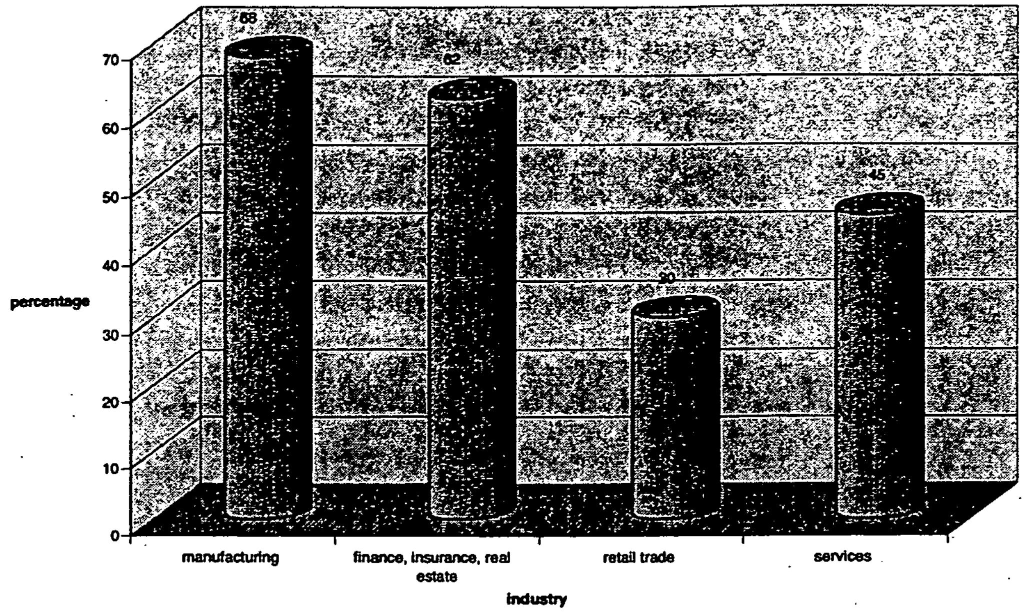
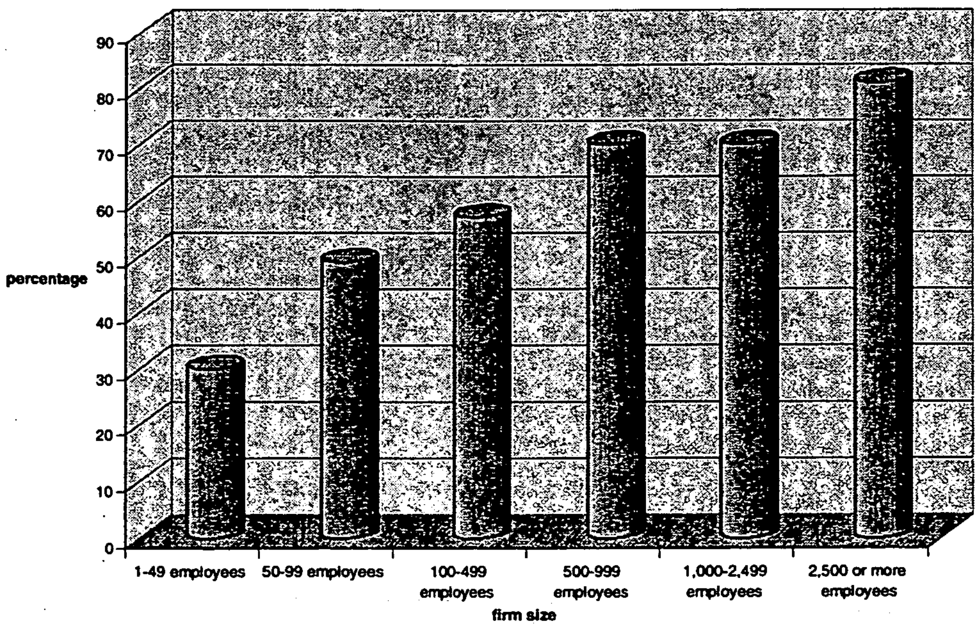


Figure 2

Percentage of Employees Participating in Employer-Sponsored Qualified Retirement Plans by Firm Size, 1999



Source: Bureau of Labor Statistics, National Compensation Survey, "Employee Benefits in Private Industry, 1999."

4. What percentage of private sector workers participating in a qualified retirement plan are only in a defined contribution plan?

In 1997, about 54 percent of workers in the private sector who participated in a qualified retirement plan were covered only by a defined contribution plan, 32 percent were covered by both a defined benefit plan and a defined contribution plan, and 14 percent were covered only by a defined benefit plan.

5. What percentage of 401(k) enrollees worked for private firms sponsoring only 401(k) plans?

In 1997, an estimated 49 percent of private sector 401(k) enrollees worked for private firms sponsoring only 401(k) plans, an increase from 46 percent in 1996 and 44 percent in 1995.

6. How have the types of qualified retirement plans that private sector employees participate in changed over time?

Figures 3 through 6 below provide a historical perspective on the growth of private sector defined contribution plans, particularly 401(k) plans, relative to defined benefit plans. The data presented in these figures are from data based on Form 5500 filings. As illustrated in the figures below, the number of defined contribution plans and active participants in those plans have increased over time, while the number of defined benefit plans and active participants in those plans has decreased. Further, the growth in defined contribution plans resulted from a large increase in 401(k) plans and participants, which offset a decrease in the number of non-401(k) defined contribution plans and participants that occurred over much of this period.

Figure 3

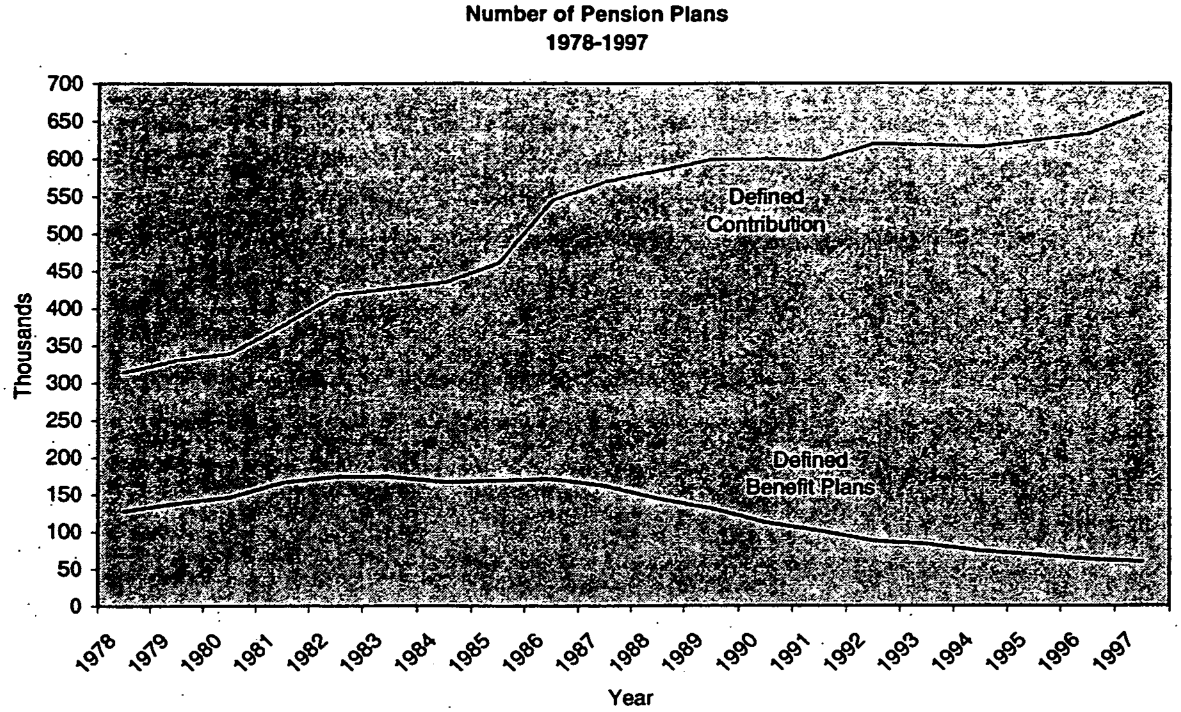


Figure 4

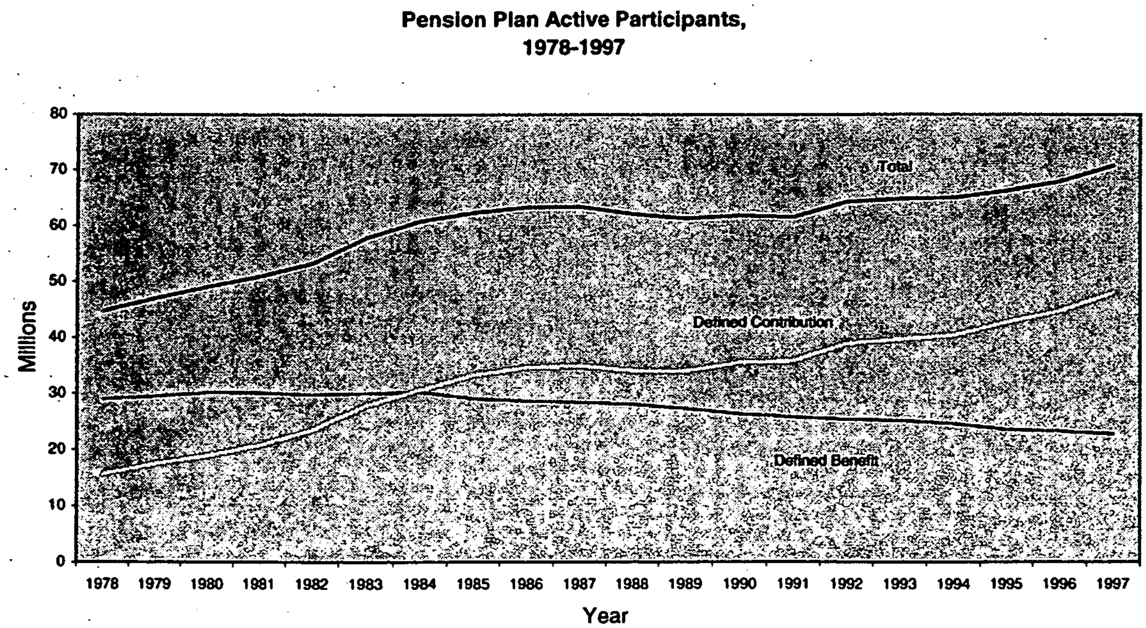


Figure 5

Number of Defined Contribution Plans
1984-1997

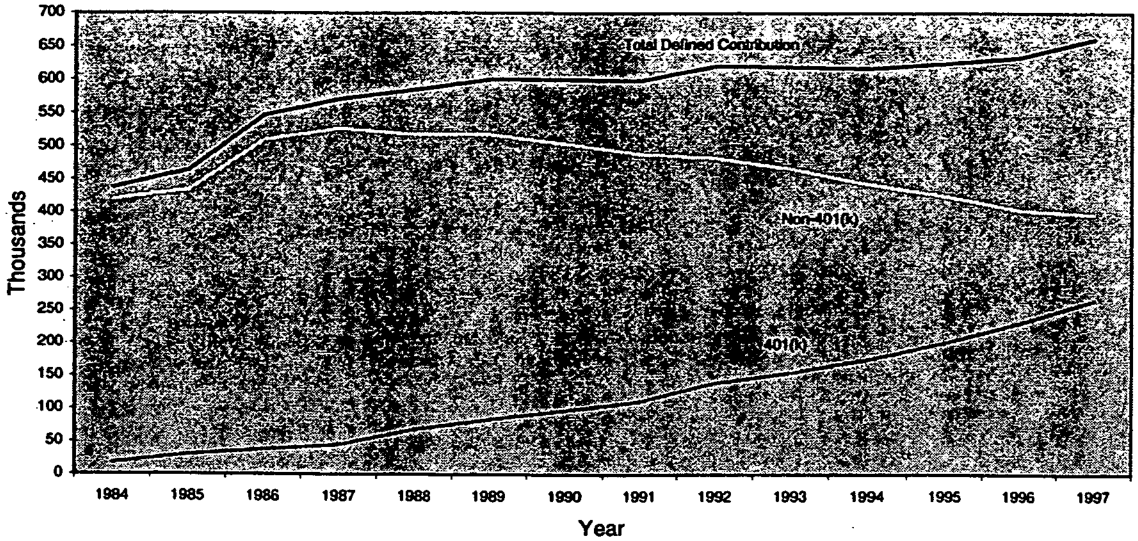
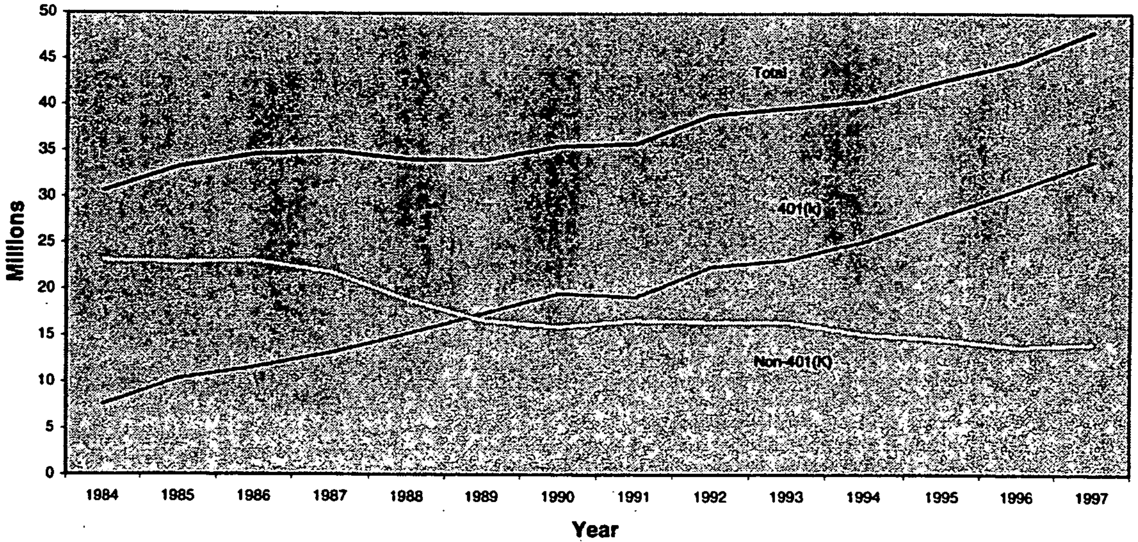


Figure 6

Active Participants in Defined Contribution Plans
1984-1997



Source for Figures 3 through 6: United States Department of Labor, Pension and Welfare Benefits Administration. Abstract of 1997 Form 5500 Annual Reports. Private Pension Plan Bulletin No. 10, Winter 2001.

7. How much money is held in employer-sponsored qualified retirement plans?

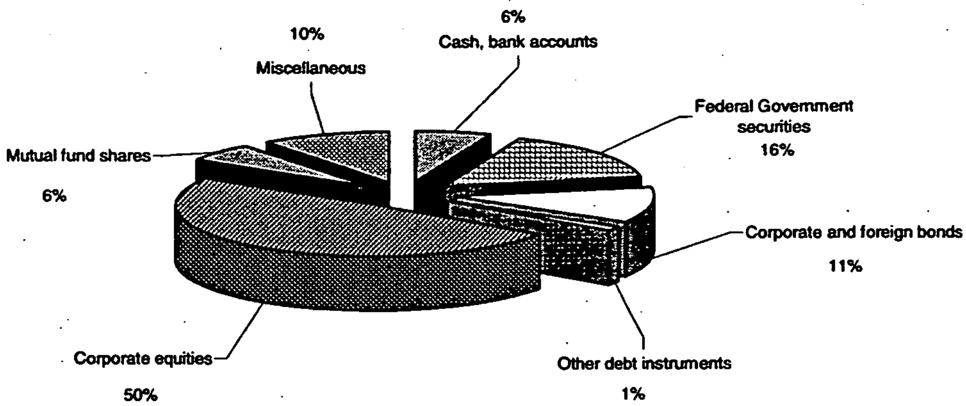
As of December 31, 2000, data from the Federal Reserve Board of Governors showed that defined benefit plans held assets valued at \$2.06 trillion and defined contribution plans held assets valued at \$2.53 trillion. In addition, individuals held assets valued at \$2.65 trillion in IRAs and Keogh accounts (i.e., qualified retirement plans for self-employed individuals).[2]

8. How are qualified retirement plan assets invested?

Figure 7 and Figure 8 below present estimates of the Federal Reserve Board of Governors of the distribution of defined benefit plan and defined contribution plan assets among different types of investments as of December 31, 2000.

Figure 7

Distribution of Assets in Defined Benefit Plans, December 31, 2000



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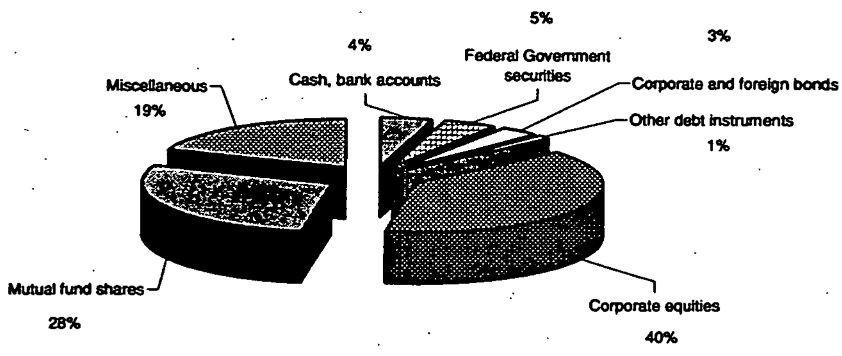
[2] Board of Governors, United States Federal Reserve System, *Flow of Funds*, December 7, 2001.

Figure 8

Distribution of Assets in Defined Contribution Plans, December 31, 2000



Source for Figures 7 and 8: Board of Governors, Federal Reserve System, *Flow of Funds*, December 7, 2001.

III. SUMMARY OF LEGISLATIVE PROPOSALS RELATING TO INVESTMENT OF DEFINED CONTRIBUTION PLAN ASSETS IN EMPLOYER STOCK

A. Proposals Relating to the Investment of Retirement Plan Assets

1. The Administration's Proposal[3]

- The proposal would permit 401(k) plan participants to sell employer stock and diversify into other investments after three years of plan participation.
- The proposal would require participants to be provided with quarterly benefit statements about their individual accounts.
- The proposal would require that participants be given 30 days notice before a blackout period begins. A "blackout period" would be a period when participants cannot control the investment of their individual accounts because of administrative changes, such as a change in plan features or plan administrator.
- The safe harbor that relieves a fiduciary from liability for investment decisions made by participants would not apply during a blackout period.
- The proposal would preclude company executives from selling their stock during a blackout period.
- The proposal would encourage employers to make investment advice available to participants and allow financial advisors to offer investment advice if agreeing to act solely in the interests of the participants.[4]

2. H.R. 3463, the Pension Protection Act (Rep. Deutsch and others)

- The bill would amend the definition of a qualified cash-or-deferred arrangement under section 401(k) of the Internal Revenue Code to add requirements related to the acquisition, holding, and divestment of employer stock.
- Employee contributions under a 401(k) plan could not be used to acquire employer stock if the acquisition would cause more than 10 percent of the fair market value of the portion of a participant's account attributable to employee contributions to consist of employer stock.
- The fair market value of employer stock held in a participant's account as of December 31 of any year could not exceed 10 percent of the fair market value of the portion of the account attributable to employee contributions.
- A participant would have to be permitted to direct the plan to divest the participant's account of employer stock that had been in the account for three years.

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[3] A detailed description of the Administration's proposal has not yet been released.

[4] The Administration has expressed support for H.R. 2269, the Retirement Security Advice Act of 2001, discussed below.

- These requirements would apply to plans on and after the date of enactment; however, employer stock held by a plan on the date of enactment would not be subject to the holding requirement.

3. H.R. 3509, the Retirement Account Protection Account of 2001 (Rep. Bentsen)

- The bill would amend the fiduciary duty provisions of ERISA to impose restrictions on "lockdowns." Accordingly, failure to comply with the lockdown requirements would be a violation of the ERISA fiduciary duty rules.
- A "lockdown" would mean any suspension of a participant's ability to transfer the participant's vested account balance out of employer stock to another investment available under the plan, but would not include a permanent limitation that applies to employer contributions invested in employer stock or a reasonable restriction on the frequency on transfers as permitted under regulations.
- A lockdown could not be imposed with respect to a participant's vested account balance unless an exemption were obtained from the Secretary of Labor and participants were given at least 60 days advance notice.
- Various notice and other procedural requirements would apply to the exemption process.
- If a plan failed to provide for compliance with the lockdown requirements, plan assets invested in employer stock would be subject to the ERISA requirements of diversification and prudence that apply to investments generally (that is, the exception to these requirements for investment in employer stock would not apply).
- The bill would also require the Secretary of Labor, in consultation with the Secretary of the Treasury and the Securities and Exchange Commission, to undertake a study relating to the investment of defined contribution plan assets in employer stock, to be submitted to Congress within 180 days after the date of enactment.
- The provisions of the bill would be effective generally for plan years beginning on or after January 1, 2002, with a delayed effective date for plans maintained pursuant to a collective bargaining agreement. A plan would not have to be amended before January 1, 2004, to comply with the bill, provided it is operated in accordance with the bill and is amended retroactively to the effective date.

4. H.R. 3622, the Emergency Worker and Investor Protection Act of 2002 (Rep. Rangel and others)

- The bill would apply the 20-percent excise tax on golden parachute payments to any amount realized by a corporate insider (within the meaning of securities laws) from a sale or exchange of stock that occurs while the corporation (or any other entity consolidated with the corporation for securities reporting purposes) maintains a "transfer-restricted 401(k) plan."
- A "transfer-restricted 401(k) plan" would mean, with respect to any period, a qualified cash-or-deferred arrangement if, during the period, any participant is not able freely to sell employer stock that is held in the participant's account and that is attributable to employee contributions, employer contributions, or earnings.

- The provision would apply to sales or exchanges of stock that occur during the six-month period beginning on the date of enactment.
- Another provision of the bill (unrelated to retirement plans) would amend the deduction rules of the Internal Revenue Code to deny a deduction for payments on certain corporate debt instruments, effective for debt instruments issued after the date of enactment.

5. H.R. 3623, the Employee Savings Protection Act of 2002 (Rep. Bentsen)

- The bill would provide that certain knowing misrepresentations by a fiduciary of a plan that included a qualified cash or deferred arrangement would constitute a breach of fiduciary duty under ERISA, and that the safe harbor that relieves a fiduciary from liability for investment decisions made by participants would not apply if such misrepresentations were made.
- The provision would apply to a knowing misrepresentation relating to the present or expected value of employer stock (1) that were made at a time reasonably contemporaneous with a period when a participant makes investment decisions with respect to his or her account or (2) that could be reasonably perceived as likely to induce investment decisions by a participant with respect to his or her account.
- The provision would apply to misrepresentations made on or after January 1, 2000.
- The bill would also amend the rules for priority claims under the Bankruptcy Code to add a priority for unsecured claims based on the knowing misrepresentation provision of ERISA, effective for bankruptcy cases commenced on or after January 1, 2000.

6. H.R. 3640, the Pension Protection and Diversification Act of 2002 (Rep. Pascrell)

- The provisions of H.R. 3640 are similar to the provisions of S. 1838, described below.

7. H.R. 3642, the 401(k) Pension Right to Know Act of 2002 (Rep. Bonior)

- The bill would amend the fiduciary duty provisions of ERISA to require an employer sponsoring a 401(k) plan to provide semiannual written notice to participants regarding the financial health of the employer and advising participants of the importance of diversifying the investment of their accounts and the risk of holding securities of any one entity, including employer stock.
- A failure to satisfy these requirements would be treated as a failure to fulfill ERISA fiduciary duties and the safe harbor that relieves a fiduciary from liability for investment decisions made by participants would not apply.
- The bill would require the first written notice pursuant to the bill to be issued within 30 days of the first day of the first plan year beginning after 60 days after the date of enactment.

8. H.R. 3657, the Employee Pension Freedom Act of 2002 (Rep. George Miller and others)

Benefit statements

- The bill would amend the reporting provisions of ERISA to require the administrator of a plan to provide periodic benefit statements and other information to plan participants.
- In the case of a single-employer plan, benefit statements would have to be provided at least every three years to defined benefit plan participants age 35 or older and at least annually to defined contribution plan participants. In the case of a multiemployer plan, a benefit statement would have to be provided at the request of a participant, but not more frequently than annually.
- The Secretary of Labor would be required to develop a model benefit statement that would provide certain information, including information about the investment of plan assets.
- In the case of a benefit distribution from a plan, on written request of the participant, the plan administrator would have to provide a worksheet explaining the calculation of the benefit amount, any documents relating to the calculation, and other information as prescribed by the Secretary. The information would be required to be provided in a form expected to be understood by the average participant.

Participant-directed investments

- Several provisions of the bill would amend the fiduciary duty provisions of ERISA to add new requirements related to participants' right to direct investments under a defined contribution plan.
- The employer and plan administrator would have a fiduciary duty to ensure that, in connection with investments made at the direction of the participant, each participant were provided with all material information that would generally be required to be disclosed by the employer to investors under securities laws. The provision of misleading information by the employer or plan administrator would be a violation of this requirement. Failure to comply with this requirement could make the employer or plan administrator subject to a civil penalty.
- The plan would be required to provide that a participant had the right to allocate the vested portion of his or her account balance that consisted of publicly-traded employer securities to any investment option under the plan. Application of a penalty or restriction based on age or service in connection with the exercise of this right generally would be a violation of this requirement. However, in the case of matching contributions under an ESOP, this right could be limited to participants with 10 years of plan participation.
- The provision would not prevent a plan from imposing a limit on what portion of a participant's account could be invested in employer securities.
- The plan administrator would be required to make the allocation to a different investment within 30 days of the participant's election or, if the plan provided for elections during prescribed periods, within 30 days of the end of the period. In addition, at least 30 days before a participant became vested (or completed 10 years

of participation in the case of an ESOP), the plan administrator would be required to notify the participant of the right to diversify the investment of his or her account and the importance of diversification.

- The Secretary of Labor would be required within a year of enactment to recommend legislative changes with respect to defined contribution plans under which participants could direct the investment of assets in their accounts and the assets in the account did not include publicly-traded employer securities.
- The bill would also impose restrictions on "lockdowns." A "lockdown" would mean a temporary freeze or suspension of a participant's ability to direct the investment of the assets in his or her account as otherwise generally provided under the plan. A lockdown could not take effect until at least 30 days written notice were provided to participants and could not continue for more than 10 consecutive business days. Subject to regulations, an exception would be provided in the case of an emergency.

Vesting of employer contributions

- The bill would amend the vesting provisions under ERISA for defined contribution plans so that the portion of a participant's account balance attributable to employer contributions would be vested after one year of service.

Other changes

- The trust requirements under ERISA would be amended to provide that, in the case of a single-employer defined contribution plan that included employee contributions, at the request of a majority of the plan participants, the assets of the plan would be required to be held in trust by a board that included trustees representing on an equal basis the interests of the employer and the interests of the participants (with a neutral party as a tie breaker). The provision would include rules for the designation or selection of the trustees to represent participants' interests.
- The bonding provision of ERISA would be amended to require that each fiduciary of a defined contribution plan be bonded or insured in an amount sufficient to cover financial losses due to any failure to satisfy the fiduciary requirements under ERISA.
- Fiduciary liability under ERISA would be extended to any person who, with notice of the facts constituting a breach of fiduciary duty by a plan fiduciary, participated in or undertook to conceal the breach. In addition, any person liable for a breach of fiduciary duty would be liable to plan participants directly.
- The civil enforcement provision of ERISA would be amended to expand the types of relief available in an action brought by a plan participant or fiduciary or the Secretary of Labor and to prevent the waiver of ERISA rights.
- A new Office of Pension Participant Advocacy would be established in the Department of Labor to handle issues and provide reports on retirement plans and plan participants.
- The Pension Benefit Guaranty Corporation would be required to undertake a study relating to the establishment of an insurance system for defined contribution plans and to report thereon within three years.

Effective date

- The provisions of the bill would be effective generally for plan years beginning on or after January 1, 2003, with a delayed effective date for plans maintained pursuant to a collective bargaining agreement. A plan could be amended retroactively to comply with the bill, provided it is operated in accordance with the bill as of the effective date and the amendment is retroactive to the effective date.

9. H.R. 3669, the Employee Retirement Savings Bill of Rights (Reps. Portman and Cardin)

Diversification requirement

- The bill would add a new diversification requirement under the Internal Revenue Code for qualified defined contribution plans holding publicly-traded employer stock.
- Under the diversification requirement, a participant could elect at least quarterly to have a certain percentage of the portion of his or her account attributable to elective deferrals transferred from employer stock and reinvested in any of at least three other investment options. The percentage would generally be phased in as follows: 20 percent for 2003, 40 percent for 2004, 60 percent for 2005, 80 percent for 2006, and 100 percent for 2007 and thereafter.
- A similar diversification requirement would apply with respect to the portion of a participant's account attributable to employer contributions invested in employer stock if the participant had at least five years of service (or three years of service in the case of employer matching contributions).
- The diversification requirement applicable to ESOPs under present law would not apply with respect to publicly traded employer stock. However, the diversification percentages under the new requirement would be coordinated the percentages applicable under present law.
- The definition of an ESOP would be amended to provide that a plan would not fail to be treated as an ESOP merely because the plan provided for the new diversification rights (or greater rights) or because participants exercised such rights.
- The new requirement would apply to plan years beginning after December 31, 2002, with an exception for certain grandfathered ESOPs.

Notice of investment principles

- The bill would amend the Internal Revenue Code to apply a new investment notice requirement in the case of a qualified retirement plan or annuity, a tax-sheltered annuity, a simplified employee pension, a SIMPLE plan, or an eligible deferred compensation plan of a governmental employer that permitted participants to direct the investment of their accounts or under which benefits depended on hypothetical investments directed by participants.
- On enrollment in the plan and at least annually thereafter, participants would have to be provided with written notice of generally accepted investment principles, including principles of risk management and diversification.
- The notice would be required to be written in a manner expected to be understood by the average participant and could be provided electronically. The Secretary of the

Treasury, in consultation with the Secretary of Labor, would be required to issue a model notice.

- The employer (or the plan in the case of a multiemployer plan) would be subject to an excise tax of $100 for a failure to provide the notice to an individual unless reasonable diligence to meet the notice requirement were exercised and notice were provided within 30 days of when the failure was discovered.
- The excise tax would be subject to an overall annual limitation of $500,000 if reasonable diligence to meet the notice requirement were exercised. The excise tax could also be waived if the failure were due to reasonable cause.
- The new requirement would be effective 60 days after the adoption of rules or other guidance (including the model notice) to implement the notice requirement. Such rules or other guidance would be required to be issued within 120 days after the date of enactment.

Notice of transaction restriction periods

- The bill would amend the Internal Revenue Code to apply another new notice requirement in the case of a qualified retirement plan or annuity, a tax-sheltered annuity, or an eligible deferred compensation plan of a governmental employer that maintained accounts for participants or under which benefits depended on hypothetical investments directed by participants.
- At least 21 days before the beginning of a "transaction restriction period," written notice of the transaction restriction period, and the effect thereof, would have to be provided to participants to whom the transaction restriction period applied, as well as any employee organization representing them. In the case of a transaction restriction period in connection with the disposition of substantially all of the stock of a subsidiary or the assets of a trade or business, notice generally would be required at least 21 days before the disposition.
- The notice would be required to be written in a manner expected to be understood by the average participant and could be provided electronically.
- A "transaction restriction period" would mean a temporary or indefinite period of at least three consecutive business days during which an individual's right to direct investments or obtains loans or distributions from the plan were substantially reduced. For this purpose, rights would be treated as substantially reduced with respect to directing investments out of employer stock if rights were significantly restricted for at least three consecutive business days.
- The employer (or the plan in the case of a multiemployer plan) would be subject to an excise tax of $100 for a failure to provide the notice to an individual unless reasonable diligence to meet the notice requirement were exercised and notice were provided as soon as reasonably practicable after the failure was discovered.
- The excise tax would be subject to an overall annual limitation of $500,000 if reasonable diligence to meet the notice requirements were exercised. The excise tax could also be waived if the failure were due to reasonable cause.
- The new requirement would apply to transaction restriction periods beginning after 60 days after the issuance of guidance to implement the notice requirement. Such guidance would be required to be issued within 60 days after the date of enactment.

Qualified retirement planning services

- The bill would expand the present-law exclusion for employer-provided qualified retirement planning services to allow employees to choose whether to receive qualified retirement planning services or other taxable compensation.
- The exclusion would be available to highly compensated employees only if a choice were available on substantially the same terms to all employees normally provided education and information on the qualified employer plan.
- The expanded exclusion would apply to years beginning after December 31, 2002.

10. H.R. 3677, the Safeguarding America's Retirement Act of 2002 (Rep. English)

- The bill would amend the ERISA provisions relating to investments in employer stock or real property to add new rules relating to the investment of 401(k) plan assets in employer stock.
- Assets attributable to employee contributions could be invested in employer stock only to the extent elected by the participant.
- In the case of a participant with less than three years of plan participation, no more than 20 percent of the participant's account attributable to employee contributions could be invested in employer stock.
- In the case of a participant with three or more years of plan participation, no more than 20 percent of the participant's entire vested account could be invested in employer stock.
- If any portion of a participant's vested account attributable to employee contributions were invested in employer stock, the participant would have to be given the opportunity at least quarterly to direct a transfer to another investment option.
- No "lockdown" could be imposed with respect to a participant's vested benefit. A "lockdown" would mean any temporary lockdown, blackout, freeze, suspension, or similar limitation on an opportunity otherwise generally available to a participant under the plan to transfer any of his or her vested account from investment in employer stock to another investment option under the plan. Lockdown would not include any reasonable restriction on the frequency of transfers between investment options.
- The bill would amend the enforcement provisions of ERISA to add criminal and civil penalties for violations of these requirements.
- The provisions of the bill would be effective generally for plan years beginning on or after January 1, 2003, with a delayed effective date for plans maintained pursuant to a collective bargaining agreement. A plan would not have to be amended before January 1, 2005, to comply with the bill, provided it is operated in accordance with the bill and is amended retroactively to the effective date.

11. H.R. 3692, the Pension Protection and Diversification Act of 2002 (Rep. Jackson-Lee)

- The provisions of H.R. 3692 are similar to the provisions of S. 1838, described below.

12. S. 1838, the Pension Protection and Diversification Act of 2001 (Sens. Boxer and Corzine)

Investment in employer stock or real property

- The bill would amend the ERISA provisions relating to investments in employer stock or real property to add requirements related to the acquisition, holding, and divestment of employer stock or real property in a defined contribution plan, other than an ESOP.
- The plan could not acquire employer stock or real property if the acquisition would cause more than 20 percent of the fair market value of a participant's account to consist of employer stock and real property.
- The fair market value of employer stock and real property held in a participant's account as of the last day of any calendar quarter could not exceed 20 percent of the fair market value of the account. Stock and real property allocated to the participant's account before the effective date would not cause the holding requirement to be violated.
- A fully vested participant would have to be permitted to direct the plan to divest the participant's account of employer stock or real property that had been in the participant's account for 90 days and reinvest an equivalent amount in other assets.
- Regulations would provide for notice to a participant if employer stock or real property had to be sold to comply with the holding requirement and for a reasonable period in which to sell employer stock or real property to comply with the holding or divestment requirement. Regulations could also waive the holding requirement where market fluctuation caused the value of employer stock or real property to exceed 20 percent of the account balance by only a de minimis amount.
- Failure to meet the acquisition, holding, or divestment requirement would mean that the plan could not acquire employer stock or real property if the acquisition would cause more than 10 percent of the fair market value of the plan's assets to consist of employer stock. This restriction would apply to the plan's assets as a whole rather than the assets in individual participants' accounts.

ESOP diversification requirements

- The present-law diversification requirements under the Internal Revenue Code would apply to any ESOP participant who were at least age 35 and had at least 5 years of plan participation.
- If the plan provided for distributions as an alternative to diversified investments, a distribution to a participant under age 55 would have to be made by direct rollover to another retirement plan or account.

Deductions

- In the case of employer matching contributions made to a defined contribution plan (other than an ESOP) in the form of employer stock, the employer's deduction would be limited to 50 percent of the amount that would otherwise be allowable.

Effective date

- The provisions of the bill would apply to years beginning on or after December 31, 2002, with a delayed effective date for plans maintained pursuant to a collective bargaining agreement.

13. S. 1919, the Retirement Security Protection Act of 2002 (Sen. Wellstone)

Investment in employer stock or real property

- The bill would amend the ERISA provisions relating to investments in employer stock or real property to add new requirements related to such investments by an "applicable individual account plan."
- An "applicable individual account plan" would mean a defined contribution plan, other than a multiemployer plan or an ESOP that (1) is maintained by an employer that has not issued any publicly traded stock or (2) holds employer stock that possesses more than 50 percent of the voting rights of all classes of employer stock or 50 percent of the value of all classes of employer stock.
- An applicable individual account plan could not acquire employer stock or real property after December 31, 2003, if the acquisition would cause a participant's "employer asset percentage" to exceed 20 percent. In addition, if, as of December 31, 2003, a participant's employer asset percentage exceeded 20 percent, the participant would have to reallocate assets to the extent needed to reduce his or her employer asset percentage to 20 percent or less by December 31, 2007.
- A participant's "employer asset percentage" would mean the ratio of (1) the fair market value of all employer stock or real property in the participant's accounts under all applicable individual account plans maintained by the employer, to (2) the sum of the fair market value of all assets in the participant's accounts under all applicable individual account plans maintained by the employer plus the present value of the participant's accrued benefits under all defined benefit plans maintained by the employer. A participant's employer asset percentage would be determined each time the assets in a participant's account were valued and at least annually.
- An exception to the 20-percent limitation would generally apply if the applicable individual account plan did not exceed the "employer asset limitation."
- Under the "employer asset limitation," the ratio of (1) the fair market value of all employer stock and real property held by all applicable individual account plans maintained by the employer, to (2) the fair market value of all assets held by all applicable individual account plans and all defined benefit plans maintained by the employer could not exceed 15 percent. For this purpose, only plans covering the same or substantially all of the same employees or group of employees as the applicable individual account plan could be taken into account.
- Regulations would provide for a reasonable period in which to sell employer stock or real property to comply with these requirements. Regulations could also waive these requirements or provide an extension of time for compliance if a failure to comply were inadvertent or attributable to a merger or acquisition or were otherwise appropriate.

- Failure to meet these requirements would mean that an applicable individual account plan could not acquire employer stock or real property if the acquisition would cause more than 10 percent of the fair market value of the plan's assets to consist of employer stock or real property.
- The bill would also require the Secretary of Labor, jointly with the Secretary of the Treasury, to undertake a study as to the application of these requirements to ESOPs that provide only for employer nonelective contributions.
- The bill would also amend the fiduciary duty provisions of ERISA to prohibit a defined contribution plan from requiring that a participant invest his or her contributions (including elective deferrals) in employer stock or real property.

Participant-directed investments

- Several provisions of the bill would amend the fiduciary duty provisions of ERISA to add new requirements related to participants' right to direct investments under a defined contribution plan.
- The employer and plan administrator would have a fiduciary duty to ensure that, in connection with investments made at the direction of the participant, each participant were provided with all material information that would generally be required to be disclosed by the employer to investors under securities laws. The provision of misleading information by the employer or plan administrator would be a violation of this requirement. Failure to comply with this requirement could make the employer or plan administrator subject to a civil penalty.
- The plan would be required to provide that, after one year of service (or 10 years of participation in the case of nonelective employer contributions to an ESOP), a participant has the right to reinvest any employer contribution of employer stock or real property in any other investment option under the plan. This requirement would apply only if the employer had issued publicly traded stock.
- The plan administrator would be required to effectuate any reinvestment of employer contributions elected by a participant within 30 days or, if the plan provided for elections during prescribed periods, within 30 days of the end of the period. In addition, at least 30 days before a participant completed one year of service (or 10 years of participation in the case of nonelective employer contributions to an ESOP), the plan administrator would be required to notify the participant of the right to reinvest the employer contributions and the importance of diversification.
- An ESOP would not be treated as failing any requirement to maintain a minimum percentage of its assets in employer stock solely by reason of a participant's election to reinvest employer stock in other assets.
- The Secretary of Labor would be required within a year of enactment to recommend legislative changes with respect to defined contribution plans under which participants may direct the investment of assets in their accounts and the assets in the account include employer stock that is not publicly traded.
- The bill would also impose restrictions on "lockdowns" in the case of a defined contribution plan that provided for investment in employer stock or real property. A "lockdown" would mean a temporary freeze or suspension of a participant's ability to

direct the investment of the assets in his or her account as otherwise generally provided under the plan.

- A lockdown could not be take effect until at least 30 days written notice were provided to participants and could not continue for more than 10 consecutive business days. Subject to regulations, an exception would be provided in the case of an emergency.
- In addition, a plan fiduciary that breached its fiduciary duty in the implementation of a lockdown would be liable for any loss resulting from a participant's inability to exercise control over employer stock or real property in his or her account by reason of the lockdown.
- The bill would also amend ERISA to prohibit directors, officers, and principal stockholders of the employer from selling employer stock during a lockdown period.

Other changes

- The annual reporting provisions of ERISA would be amended to provide that a public accountant examining a plan's financial records and statements would not be treated as independent if the accountant (or the accountant's firm) were employed by or performed compensated services for the employer maintaining the plan.
- The fiduciary liability and enforcement provisions of ERISA would be amended to expand the types of relief available in an action brought by a plan participant or fiduciary or the Secretary of Labor, to prevent the waiver of ERISA rights, and to provide additional protections against interference with participants' rights.
- The bill also contains provisions relating to the following, which are similar to the provisions of H.R. 3657, described above: (1) a requirement that participants be provided with periodic benefit statements, (2) a requirement that the board of trustees represent the interests of the employer and participants on an equal basis, (3) new bonding and insurance requirements, (4) new fiduciary liability for any person involved in the concealment of a breach of fiduciary duty, (5) the establishment of a new Office of Pension Participant Advocacy in the Department of Labor, and (6) a study by the Pension Benefit Guaranty Corporation relating to the establishment of an insurance system for defined contribution plans.

Effective date

- The provisions of the bill would be effective generally for plan years beginning on or after January 1, 2003, with a delayed effective date for plans maintained pursuant to a collective bargaining agreement. A plan could be amended retroactively to comply with the bill, provided it is operated in accordance with the bill as of the effective date and the amendment is retroactive to the effective date.

14. S. 1921, the Pension Plan Protection Act (Sens. Hutchison, Lott, and Craig)

Diversification requirement for applicable defined contribution plans

- The bill would amend the Internal Revenue Code to add new qualification requirements relating to diversification of assets in the case of an "applicable defined contribution plan."
- An "applicable defined contribution plan" would mean a defined contribution plan, other than an ESOP that provided only for employer nonelective contributions. (The ESOP diversification requirements under present law would no longer apply to an ESOP that is an applicable defined contribution plan.)
- The plan would have to provide participants with at least four different investment options, including three that do not involve employer stock or real property.
- The plan would have to provide that no employee contributions (including elective deferrals) could be required to be invested in employer stock or employer real property.
- A fully vested participant would have to be permitted to direct the plan to divest the participant's account of employer stock or real property that had been in the participant's account for 90 days and reinvest an equivalent amount in other assets. Regulations would provide for a reasonable period in which to sell employer stock or real property to comply with this requirement.
- The bill would amend the fiduciary duty provisions of ERISA to add similar requirements.

Benefit statements

- The plan administrator of an applicable defined contribution plan would be required to provide quarterly statements to participants about their accounts, including the fair market value of the assets in each investment option and the percentage of the account invested in each option. Regulations could provide an exception for plans with fewer than 100 participants.
- If more than 25 percent of the fair market value of a participant's account consisted of employer stock, the plan administrator would have to provide a separate notice of that percentage and a reminder of the need for diversification and a recommendation that the participant seek investment advice.
- The notices would be required to be written in a manner expected to be understood by the average plan participant.
- The employer (or the plan in the case of a multiemployer plan) would be subject to an excise tax in the case of a failure to provide the required benefit statements. In general, the excise tax would be $100 a day (subject to an overall limitation) until the notice were provided or the failure otherwise corrected.
- The bill would amend the provisions of ERISA dealing with the furnishing of information to participants to add similar requirements for quarterly benefit statements.

Blackouts

- A "blackout" would mean any temporary blackout, lockdown, suspension, or similar limitation within the control of the employer or the plan administrator with respect to a participant's ability to transfer any of his or her vested benefit from investment in employer stock to another investment option under the plan. A blackout would not include any permanent limitation that applied only to benefits attributable to employer contributions or any reasonable restriction on the frequency of transfers between investment options.
- An applicable defined contribution plan would be required to provide that a blackout could not take effect until at least 30 days written notice had been provided to participants.
- The employer (or the plan in the case of a multiemployer plan) would be subject to an excise tax in the case of a failure to provide the required blackout notice. In general, the excise tax would be $100 a day (subject to an overall limitation) until the notice were provided or the failure otherwise corrected.
- The bill would also amend the fiduciary duty provisions of ERISA to apply similar blackout restrictions. In addition, a plan fiduciary that breached its fiduciary duty with respect to the imposition of a blackout or a participant's ability to exercise control over assets during the blackout would be liable for any loss during the blackout from the investment of the participant's assets in employer stock or real property.
- The bill would also amend the Securities Exchange Act to prohibit a beneficial owner, director or officer of the employer from selling employer stock during a blackout period.

Other provisions

- The bill also contains investment advice provisions similar to those contained in H.R. 2269, described below.
- The bill would also require the Secretary of Labor, in consultation with the Secretary of the Treasury and the Securities and Exchange Commission, to undertake a study relating to the investment of defined contribution plan assets in stock or other securities, to be submitted to Congress within 180 days after the date of enactment.
- The bill would also amend the Securities Exchange Act to limit a public accountant's ability to provide auditing services and other services for the same entity.

Effective date

- The provisions of the bill would be effective generally for plan years beginning on or after January 1, 2002, with a delayed effective date for plans maintained pursuant to a collective bargaining agreement. A plan could be amended retroactively to comply with the bill, provided it is operated in accordance with the bill as of the effective date and the amendment is retroactive to the effective date.

B. Proposals Relating to Investment Advice

1. H.R. 2269, the Retirement Security Advice Act of 2001 (passed by the House on November 15, 2001)

- The bill would amend the prohibited transaction rules under ERISA and the Internal Revenue Code to provide an exemption for (1) the provision of investment advice to the plan or plan participants with respect to the investment of plan assets, (2) the sale, acquisition or holding of investments pursuant to the advice, and (3) the receipt of fees for the advice or the investments.
- The exemption would apply to plans under which the investment of plan assets is subject to the direction of plan participants and to investments made solely at the direction of the recipient of the investment advice.
- The exemption would apply to an investment advisor who is a "fiduciary advisor," defined as a person who is a fiduciary of the plan by reason of the provision of investment advice and who is also (1) a registered investment adviser, (2) a bank, (3) an insurance company, (4) a registered broker or dealer, or (5) an affiliate, employee, agent, or registered representative of such an entity.
- The investment advisor would have to provide a plain-language notice that includes information about (1) fees to be received by the advisor in connection with the advice or the investments, (2) the types of services provided by the advisor, (3) any limitations on the scope of the investment advice, and (4) any connection between the advisor and the investments. The investment advisor would also have to acknowledge its status as a fiduciary of the plan.
- The notice would have to be provided at the time of the initial investment advice and at least annually after. This notice would be in addition to notices required under other laws, such as securities laws.
- Any fees received by the investment advisor would have to be reasonable, and the terms of any investments would have to be at least as favorable as an arm's length transaction would be.
- If the requirements for the exemption were met, the employer (or other fiduciary) would not be responsible under ERISA for the investment advice provided by the fiduciary advisor. The employer or other fiduciary would continue to bear fiduciary responsibility for selecting and monitoring the fiduciary advisor.
- The bill would also amend ERISA to clarify that plan assets may be used to pay reasonable expenses for investment advice.
- The bill would apply to advice provided on or after January 1, 2002.

2. S. 1677, the Independent Investment Advice Act of 2001 (Sens. Bingaman and Collins)

- The bill would amend ERISA by adding specific rules dealing with the provision of investment advice to plan participants.
- The proposal would apply to a defined contribution plan that permits participants to exercise investment control over the assets in their accounts and to investment advice provided to participants by a qualified investment advisor.

- A "qualified investment advisor," would be defined as a person who is a plan fiduciary by reason of providing investment advice and who is also (1) a registered investment adviser, (2) a bank, (3) an insurance company, or (4) a comparably qualified entity under criteria to be established by the Secretary of Labor. Similar requirements would apply to any individual who provided investment advice to participants on behalf of the investment advisor (such as an employee thereof).
- In designating an investment advisor, the employer or other fiduciary would be required to review (1) the contract for investment advice services, (2) the fees to be received by the investment advisor, and (3) documentation that the investment advisor is a qualified investment advisor. The employer or other fiduciary would also make a determination that there is no material reason not to engage the investment advisor.
- Before designating the investment advisor and at least annually thereafter, the employer or other fiduciary would be required to obtain written verification that the investment advisor (1) is a qualified investment advisor, (2) acknowledges its status as a plan fiduciary that is solely responsible for the investment advice it provides, (3) has reviewed the plan document (including investment options) and determined that it can provide investment advice to participants without violating the prohibited transaction rules, and (4) has sufficient insurance to cover claims by participants.
- If questions were raised about the investment advisor's qualified status or about the quality of its services, the employer or other fiduciary would be required to determine within 30 days whether to continue the investment advisor's services.
- An employer or other fiduciary that complied with the requirements for designating and monitoring an investment advisor would be deemed to have satisfied its fiduciary duty in the prudent selection and review of an investment advisor and would not bear fiduciary liability for any loss or breach resulting from the investment advice.
- The bill would also amend ERISA to provide that amounts recovered by the plan for a breach of fiduciary duty by a qualified investment advisor would benefit the accounts of the plan participants affected by the breach.
- The bill would apply with respect to investment advisors designated on or after the date of enactment.

DESCRIPTION OF S. ______
"ENERGY TAX INCENTIVES ACT OF 2002"

Scheduled for Markup
by the
Senate Finance Committee
on February 13, 2002

Prepared by
the Staff of the
JOINT COMMTTEE ON TAXATION

February 11, 2002
JCX-2-02

CONTENTS

INTRODUCTION

The Senate Committee on Finance has scheduled a markup on February 13, 2002, of S. _____ "Energy Tax Incentives Act of 2002." This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the "Energy Tax Incentives Act of 2002."

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[1] This document may be cited as follows: Joint Committee on Taxation, *Description of S. ______, "Energy Tax Incentives Act of 2002"* (JCX-2-02), February 11, 2002.

I. RENEWABLE ENERGY

A. Extension and Modification of the Section 45 Electricity Production Credit

Present Law

An income tax credit is allowed for the production of electricity from either qualified wind energy, qualified "closed-loop" biomass, or qualified poultry waste facilities (sec. 45). The amount of the credit is 1.5 cents per kilowatt hour (indexed for inflation) of electricity produced. The amount of the credit was 1.7 cents per kilowatt hour for 2001. The credit is reduced for grants, tax-exempt bonds, subsidized energy financing, and other credits.

The credit applies to electricity produced by a wind energy facility placed in service after December 31, 1993, and before January 1, 2002, to electricity produced by a closed-loop biomass facility placed in service after December 31, 1992, and before January 1, 2002, and to a poultry waste facility placed in service after December 31, 1999, and before January 1, 2002. The credit is allowable for production during the 10-year period after a facility is originally placed in service. In order to claim the credit, a taxpayer must own the facility and sell the electricity produced by the facility to an unrelated party. In the case of a poultry waste facility, the taxpayer may claim the credit as a lessee/operator of a facility owned by a governmental unit.

Closed-loop biomass is plant matter, where the plants are grown for the sole purpose of being used to generate electricity. It does not include waste materials (including, but not limited to, scrap wood, manure, and municipal or agricultural waste). The credit also is not available to taxpayers who use standing timber to produce electricity. Poultry waste means poultry manure and litter, including wood shavings, straw, rice hulls, and other bedding material for the disposition of manure.

The credit for electricity produced from wind, closed-loop biomass, or poultry waste is a component of the general business credit (sec. 38(b)(8)). The credit, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000, or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39). To coordinate the carryback with the period of application for this credit, the credit for electricity produced from closed-loop biomass facilities may not be carried back to a tax year ending before 1993 and the credit for electricity produced from wind energy may not be carried back to a tax year ending before 1994 (sec. 39).

Description of Proposal

The proposal would extend the placed in service date for wind facilities, closed-loop biomass facilities, and poultry waste facilities to facilities placed in service after December 31, 1993 (December 31, 1992 in the case of closed-loop biomass facilities and December 31, 1999 in the case of poultry waste facilities) and before January 1, 2007.

The proposal also would define three new qualifying energy resources: open-loop biomass, swine and bovine waste nutrients, and geothermal energy. Open-loop biomass would be defined as any solid, nonhazardous, cellulosic waste material which is segregated from other waste materials and which is derived from any of forest-related resources, solid wood waste materials, or agricultural sources. Eligible forest-related resources would be defined as mill residues, precommercial thinnings, slash, and brush, but not including old-growth timber. Solid wood waste materials would include waste pallets, crates, dunnage, manufacturing and construction wood wastes (other than pressure-treated, chemically-treated, or painted wood wastes), and landscape or right-of-way tree trimmings. Agricultural sources would include orchard tree crops, vineyard, grain, legumes, sugar, and other crop by-products or residues. However, qualifying open-loop biomass would not include municipal solid waste (garbage), gas derived from biodegradation of solid waste, or paper that is commonly recycled. Swine and bovine waste nutrients would be defined as swine and bovine manure and litter, including bedding material for the disposition of manure. Geothermal energy would be defined as energy derived from a geothermal deposit which is a geothermal reservoir consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor (whether or not under pressure).

Qualifying open-loop biomass facilities would be facilities using open-loop biomass to produce electricity that are placed in service prior to January 1, 2005. Qualifying swine and bovine waste nutrient facilities would be facilities using swine and bovine waste nutrients to produce electricity that are placed in service after the date of enactment and before January 1, 2007. Qualifying geothermal energy facilities would be facilities using geothermal deposits to produce electricity that are placed in service after the date of enactment and before January 1, 2007.

In the case of qualifying open-loop biomass facilities, taxpayers would be able to claim the otherwise allowable credit for a three-year period. For facilities placed in service after the date of enactment, the three-year period would commence when the facility is placed in service. In the case of open-loop biomass facilities originally placed in service before the date of enactment, the three-year period would commence after December 31, 2002 and the otherwise allowable 1.5 cent-per-kilowatt-hour credit (adjusted for inflation) would be reduced to 1.0 cent-per-kilowatt-hour credit (adjusted for inflation). In the case of qualifying geothermal energy facilities, taxpayers would be able to claim the otherwise allowable credit for the five-year period commencing when the facility is placed service.

The proposal would modify present law to provide that qualifying closed-loop biomass facilities include any facility originally placed in service before December 31, 1992 and modified to use closed-loop biomass to co-fire with coal before January 1, 2007.

In the case of qualifying open-loop biomass facilities and qualifying closed-loop biomass facilities modified to use closed-loop biomass to co-fire with coal, the proposal would permit a lessee operator to claim the credit in lieu of the owner of the facilities.

The proposal would provide that certain persons (public utilities, electric cooperatives, rural electric cooperatives, and Indian tribes) could sell, trade, or assign to any taxpayer any credits that would otherwise be allowable to that person, if that person were a taxpayer, for production of electricity from a qualified facility owned by such person. In addition, any credits that would otherwise be allowable to such person may be applied as a prepayment to certain loans or obligations undertaken by such person under the Rural Electrification Act of 1936.

Lastly, the proposal would repeal the present-law reduction in allowable credit for facilities financed with tax-exempt bonds or with certain loans received under the Rural Electrification Act of 1936.

Effective Date

The proposal generally would be effective for electricity sold from qualifying facilities after the date of enactment. For electricity produced from qualifying open-loop biomass facilities originally placed in service prior to the date of enactment, the proposal would be effective January 1, 2003.

II. ALTERNATIVE VEHICLES AND FUEL INCENTIVES

A. Modifications and Extensions of Provisions Relating to Electric Vehicles, Clean-Fuel Vehicles, and Clean-Fuel Vehicle Refueling Property

Present Law

A 10-percent tax credit is provided for the cost of a qualified electric vehicle, up to a maximum credit of $4,000 (sec. 30). A qualified electric vehicle is a motor vehicle that is powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells, or other portable sources of electrical current, the original use of which commences with the taxpayer, and that is acquired for the use by the taxpayer and not for resale. The full amount of the credit is available for purchases prior to 2002. The credit phases down in the years 2002 through 2004, and is unavailable for purchases after December 31, 2004. There is no carry forward or carryback of the credit for electric vehicles.

Certain costs of qualified clean-fuel vehicle property and clean-fuel vehicle refueling property may be expensed and deducted when such property is placed in service (sec. 179A). Qualified clean-fuel vehicle property includes motor vehicles that use certain clean-burning fuels (natural gas, liquefied natural gas, liquefied petroleum gas, hydrogen, electricity and any other fuel at least 85 percent of which is methanol, ethanol, or any other alcohol or ether). The maximum amount of the deduction is $50,000 for a truck or van with a gross vehicle weight over 26,000 pounds or a bus with seating capacities of at least 20 adults; $5,000 in the case of a truck or van with a gross vehicle weight between 10,000 and 26,000 pounds; and $2,000 in the case of any other motor vehicle. Qualified electric vehicles do not qualify for the clean-fuel vehicle deduction.

Clean-fuel vehicle refueling property comprises property for the storage or dispensing of a clean-burning fuel, if the storage or dispensing is the point at which the fuel is delivered into the fuel tank of a motor vehicle. Clean-fuel vehicle refueling property also includes property for the recharging of electric vehicles, but only if the property is located at a point where the electric vehicle is recharged. Up to $100,000 of such property at each location owned by the taxpayer may be expensed with respect to that location.

The deduction phases down in the years 2002 through 2004, and is unavailable for purchases after December 31, 2004.

Description of Proposal

Alternative motor vehicle credits

The proposal would provide a credit to the taxpayer for the purchase of a new qualified fuel cell motor vehicle, a new qualified alternative fuel motor vehicle, and a new qualified hybrid motor vehicle. The taxpayer would be able to carry forward unused credits for 20 years or carry unused credits back for three years (but not carried back to taxable years beginning before the January 1, 2003). In the case of property purchased by tax-exempt persons, the seller may claim the credit. In addition to the specifications described below, a qualifying vehicle would have to meet certain emissions standards.

Fuel cell motor vehicles

The credit for the purchase of new qualified fuel cell motor vehicles generally ranges between $4,000 and $40,000 depending upon the weight class of the vehicle. For automobiles and light trucks, the otherwise allowable credit amount ($4,000) is increased by an amount from $1,000 to $4,000 depending upon the vehicle's fuel efficiency compared to a stated standard. Credit may not be claimed for qualified fuel cell motor vehicles purchased after December 31, 2011. The taxpayer's basis in the property is reduced by the amount of credit claimed.

Hybrid motor vehicles

The credit for the purchase of a new qualified hybrid motor vehicle generally ranges from $250 to $10,000 depending upon the weight of the vehicle and the maximum power available from the vehicle's battery system. For automobiles and light trucks, the otherwise allowable credit amount ($250 to $1,000) is increased by an amount from $1,000 to $3,500 depending upon the vehicle's fuel efficiency. For heavy duty hybrid motor vehicles, the otherwise allowable credit ($1,000 to $10,000) is increased depending upon the vehicle's weight and provided the vehicle meets certain 2007 (and beyond) emissions standards. The amount of credit is increased by between $3,000 and $12,000 for vehicles placed in service in 2003, is increased by between $2,500 and $10,000 for vehicles placed in service in 2004, is increased by between $2,000 and $8,000 for vehicles placed in service in 2005, and is increased by between $1,500 and $6,000 for vehicles placed in service in 2006. Credit may not be claimed for qualified hybrid motor vehicles purchased after December 31, 2006. The taxpayer's basis in the property is reduced by the amount of credit claimed.

Alternative fuel motor vehicles

The credit for the purchase of a new alternative fuel motor vehicle equals 40 percent of the incremental cost of such vehicle, plus an additional 30 percent if the vehicle meets certain emissions standards. For computation of the credit, incremental costs of the vehicle may not exceed between $5,000 and $40,000 depending upon the weight of the vehicle. For this purpose, incremental cost generally would be defined as the amount of the increase of the cost of such a vehicle compared to the cost of a comparable gasoline or diesel model. Qualifying alternative fuels are compressed natural gas, liquefied natural gas, liquefied petroleum gas, hydrogen, and any liquid mixture consisting of at least 85 percent methanol.

Certain mixed-fuel vehicles also could claim the alternative fuel motor vehicle credit, at a reduced rate. A mixed-fuel vehicle is a vehicle with gross weight of seven tons or more and is certified by the manufacturer as being able to operate on a combination of alternative fuel and a petroleum-based fuel. A qualifying mixed-fuel vehicle must use at least 75 percent alternative fuel (a "75/25 mixed-fuel vehicle") or 90 percent alternative fuel (a "90/10 mixed-fuel vehicle") and is incapable of operating on a mixture containing less than 75 percent alternative fuel in the case of a 75/25 vehicle (less than 90 percent alternative fuel in the case of a 90/10 vehicle. A taxpayer purchasing a 75/25 mixed-fuel vehicle may claim 70 percent of the otherwise allowable credit. A taxpayer purchasing a 90/10 mixed-fuel vehicle may claim 90 percent of the otherwise allowable credit.

Credit may not be claimed for qualified alternative fuel motor vehicles purchased after December 31, 2006. The taxpayer's basis in the property is reduced by the amount of credit claimed.

Modification of credit for qualified electric vehicles

The proposal would modify the present-law credit for electric vehicles to provide that the credit for qualifying vehicles generally ranges between $3,500 and $40,000 depending upon the weight of the vehicle and, for certain vehicles, the driving range of the vehicle. In the case of property purchased by tax-exempt persons, the seller may claim the credit. The taxpayer would be ineligible for the deduction allowable under present-law section 179A for a qualified battery electric vehicle on which a credit is allowable. The proposal also would extend the expiration date of the credit from December 31, 2004 to December 31, 2006 and would repeal the phaseout schedule of present law. The taxpayer would be able to carry forward unused credits for 20 years or carry unused credits back for three years (but not carried back to taxable years beginning before the January 1, 2003).

Extension of present-law section 179A

The proposal would extend the deduction for costs of qualified clean-fuel vehicle property and clean-fuel vehicle refueling property through December 31, 2006. The phase-down of present law for clean fuel vehicles would be modified such that the taxpayer may claim 75 percent of the otherwise allowable deduction in 2003 and 2004, 50 percent of the otherwise allowable deduction in 2005, and 75 percent of the otherwise allowable deduction in 2006.

Credit for installation of alternative fueling stations

The proposal would permit taxpayers to claim a 50-percent credit for the cost of installing clean-fuel vehicle refueling property to be used in a trade or business of the taxpayer or installed at the principal residence of the taxpayer. In the case of retail clean-fuel vehicle refueling property the allowable credit could not exceed $30,000. In the case of residential clean-fuel vehicle refueling property the allowable credit could not exceed $1,000. The taxpayer's basis in the property would be reduced by the amount of the credit and the taxpayer could not claim deductions under section 179A with respect to property for which the credit is claimed. In the case of refueling property installed on property owned or used by a tax-exempt person, the taxpayer that installs the property may claim the credit. To be eligible for the credit, the property must be placed in service before January 1, 2007. Taxpayers would be able to carry forward unused credits for 20 years.

Credit for retail sale of alternative fuels

The proposal would permit taxpayers to claim a credit equal to the gasoline gallon equivalent of 30 cents per gallon of alternative fuel sold in 2003, 40 cents per gallon in 2004, and 50 cents per gallon thereafter. Qualifying alternative fuels are compressed natural gas, liquefied natural gas, liquefied petroleum gas, hydrogen, any liquid mixture consisting of at least 85 percent methanol, and any liquid mixture consisting of at least 85 percent ethanol. The gasoline gallon equivalency of any alternative fuel is determined by reference to the British thermal unit content of the alternative fuel compared to a gallon of gasoline. The credit may be claimed for sales prior to January 1, 2007. The credit would be part of the general business credit.

Effective Date

The proposals relating to the credit for new fuel cell motor vehicles, hybrid motor vehicles, and alternative fuel motor vehicles, the credit for battery electric vehicles, the credit for alternative fuel vehicle refueling property, and deductions clean fuel vehicles and clean fuel refueling property would apply to property placed in service after December 31, 2002, in taxable years ending after December 31, 2002. The credit for retail sales of alternative fuels would apply to sales of fuels after December 31, 2002, in taxable years ending after December 31, 2002.

B. Modifications to Small Producer Ethanol Credit

Present Law

Small producer credit

Present law provides several tax benefits for ethanol and methanol produced from renewable sources (e.g., biomass) that are used as a motor fuel or that are blended with other fuels (e.g., gasoline) for such a use. In the case of ethanol, a separate 10-cents-per-gallon credit for small producers, defined generally as persons whose production does not exceed 15 million gallons per year and whose production capacity does not exceed 30 million gallons per year. The alcohol fuels tax credits are includible in income. This credit, like tax credits generally, may not be used to offset alternative minimum tax liability. The credit is a treated as a general business credit, subject to the ordering rules and carryforward/carryback rules that apply to business credits generally. The alcohol fuels tax credit is scheduled to expire after December 31, 2007.

Taxation of cooperatives and their patrons

Under present law, cooperatives in essence are treated as pass-through entities in that the cooperative is not subject to corporate income tax to the extent the cooperative timely pays patronage dividends. Under present law (sec. 38(d)(4)), the only excess credits that may be flowed-through to cooperative patrons are the rehabilitation credit (sec. 47), the energy property credit (sec. 48(a)), and the reforestation credit (sec. 48(b)).

Description of Proposal

The proposal would make several modifications to the rules governing the small producer ethanol credit. First, the proposal would liberalize the definition of an eligible small producer to include persons whose production capacity does not exceed 60 million gallons. Second, the proposal would allow cooperatives to elect to pass-through the small ethanol producer credits to its patrons. The credit allowed to a particular patron would be that proportion of the credit that the cooperative elects to pass-through for that year as the amount of patronage of that patron for that year bears to total patronage of all patrons for that year.

Third, the proposal would repeal the rule that includes the small producer credit in income of taxpayers claiming it and would liberalize the ordering and carryforward/carryback rules for the small producer ethanol credit. Fourth, the proposal would allow the small producer credit to be claimed against the alternative minimum tax. Finally, the proposal would provide that the small producer ethanol credit would not be treated as derived from a passive activity under the Code rules restricting credits and deductions attributable to such activities.

Effective Date

The proposal would be effective for taxable years beginning after date of enactment.

C. Transfer Full Amount of Excise Tax Imposed on Gasohol to the Highway Trust Fund

Present Law

An 18.4 cents-per-gallon excise tax is imposed on gasoline. The tax is imposed when the fuel is removed from a refinery unless the removal is to a bulk transportation facility (e.g., removal by pipeline or barge to a registered terminal). In the case gasoline removed in bulk by registered parties, tax is imposed when the gasoline is removed from the terminal facility, typically by truck (i.e., "breaks bulk"). If gasoline is sold to an unregistered party before it is removed from a terminal, tax is imposed on that sale. When the gasoline subsequently breaks bulk, a second tax is imposed. The payor of the second tax may file a refund claim if it can prove payment of the first tax. The party liable for payment of the gasoline excise tax is called a "position holder," defined as the owner of record inside the refinery or terminal facility.

A 53-cents-per-gallon income tax credit is allowed for ethanol used as a motor fuel (the "alcohol fuels credit"). The benefit of the alcohol fuels tax credit may be claimed as a reduction in excise tax payments when the ethanol is blended with gasoline ("gasohol"). The reduction is based on the amount of ethanol contained in the gasohol. The excise tax benefits apply to gasohol blends of 90 percent gasoline/10 percent ethanol, 92.3 percent gasoline/7.7 percent ethanol, or 94.3 percent gasoline/5.7 percent ethanol. The income tax credit is based on the amount of alcohol contained in the blended fuel.

In general, 18.3 cents per gallon of the gasoline excise tax is deposited in the Highway Trust Fund and 0.1 cent per gallon is deposited in the Leaking Underground Storage Tank Trust Fund (the "LUST" rate). In the case of gasohol with respect to which a reduced excise tax is paid, 2.5 cents per gallon of the reduced tax is retained in the General Fund. The balance of the reduced rate (less the LUST rate) is deposited in the Highway Trust Fund.

Description of Proposal

The proposal would transfer the 2.5 cents per gallon of excise tax on gasohol that currently is retained in the General Fund to the Highway Trust Fund.

Effective Date

The proposal would be effective taxes imposed after September 31, 2003.

D. Modify Income Tax and Excise Tax Rules Governing Treatment of ETBE

Present Law

An 18.4 cents-per-gallon excise tax is imposed on gasoline. The tax is imposed when the fuel is removed from a refinery unless the removal is to a bulk transportation facility (e.g., removal by pipeline or barge to a registered terminal). In the case gasoline removed in bulk by registered parties, tax is imposed when the gasoline is removed from the terminal facility, typically by truck (i.e., "breaks bulk"). If gasoline is sold to an unregistered party before it is removed from a terminal, tax is imposed on that sale. When the gasoline subsequently breaks bulk, a second tax is imposed. The payor of the second tax may file a refund claim if it can prove payment of the first tax. The party liable for payment of the gasoline excise tax is called a "position holder," defined as the owner of record inside the refinery or terminal facility.

A 53-cents-per-gallon income tax credit is allowed for ethanol used as a motor fuel (the "alcohol fuels credit"). The benefit of the alcohol fuels tax credit may be claimed as a reduction in excise tax payments when the ethanol is blended with gasoline ("gasohol"). The reduction is based on the amount of ethanol contained in the gasohol. The excise tax benefits apply to gasohol blends of 90 percent gasoline/10 percent ethanol, 92.3 percent gasoline/7.7 percent ethanol, or 94.3 percent gasoline/5.7 percent ethanol. The income tax credit is based on the amount of alcohol contained in the blended fuel.

ETBE is an ether that is manufactured using ethanol. Unlike ethanol, ETBE can be blended with gasoline before the gasoline enters a pipeline because ETBE does not result in contamination of fuel with water while in transport. Treasury Department regulations provide that gasohol blenders may claim the income tax credit and excise tax rate reductions for ethanol used in the production of ETBE. The regulations also a special election allowing refiners to claim the benefit of the excise tax rate reduction even though the fuel being removed from terminals does not contain the requisite percentages of ethanol for claiming the excise tax rate reduction.

Description of Proposal

The proposal would replace the present-law regulatory procedures enabling refiners to claim excise tax benefits on ETBE-blended gasohol with a new excise tax credit alternative to the alcohol fuels income tax credit. Under the proposal, in lieu of excise tax rate reductions for specified gasohol blends, a refiner blending ETBE and ethanol would accrue an excise tax credit equal to the amount of the alcohol fuels credit or excise tax rate reduction otherwise available for the ETBE blended fuel. The refiner could use this credit to offset its excise tax liability for highway motor fuels under Code section 4081. Alternatively, the credit could be transferred to a registered position holder that is a member of the same controlled group as the refiner, and the position holder could use the excise tax credit to offset its liability for excise taxes under those Code sections.

Effective Date

The proposal would be effective for fuels blended after date of enactment.

III. CONSERVATION AND ENERGY EFFICIENCY PROVISIONS

A. Business Credit for Construction of New Energy-Efficient Homes

Present Law

A nonrefundable, 10-percent business energy credit is allowed for the cost of new property that is equipment (1) that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat, or (2) used to produce, distribute, or use energy derived from a geothermal deposit, but only, in the case of electricity generated by geothermal power, up to the electric transmission stage.

The business energy tax credits are components of the general business credit (sec. 38(b)(1)). The business energy tax credits, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000 or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39).

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present-law credit for the construction of new energy-efficient homes.

Description of Proposal

The proposal would provide a credit to an eligible contractor of an amount equal to the aggregate adjusted bases of all energy-efficient property installed in a qualified new energy-efficient home during construction. The credit cannot exceed $1,250 ($2,000) in the case of a new home which has a projected level of annual heating and cooling costs that is 30 percent (50 percent) less than a comparable dwelling constructed in accordance with Chapter 4 of the 2000 International Energy Conservation Code.

The eligible contractor would be the person who constructed the home, or in the case of a manufactured home, the producer of such home. Energy efficiency property would be any energy-efficient building envelope component (insulation materials or system designed to reduce heat loss or gain, and exterior windows, including skylights, and doors) and any energy-efficient heating or cooling appliance that can, individually or in combination with other components, meet the standards for the home.

To qualify as an energy-efficient new home, the home must be: (1) a dwelling located in the United States; (2) the principal residence of the person who acquires the dwelling from the eligible contractor; and (3) certified to have a projected level of annual heating and cooling energy consumption that meets the standards for either the 30-percent or 50-percent credit. The home may be certified according to a component-based method or an energy performance based method.

Effective Date

The credit applies to homes whose construction is substantially completed after the date of enactment and which are purchased during the period beginning on the date of enactment and ending on December 31, 2007.

B. Tax Credit for Energy-Efficient Appliances

Present Law

A nonrefundable, 10-percent business energy credit is allowed for the cost of new property that is equipment: (1) that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat; or (2) used to produce, distribute, or use energy derived from a geothermal deposit, but only, in the case of electricity generated by geothermal power, up to the electric transmission stage.

The business energy tax credits are components of the general business credit (sec. 38(b)(1)). The business energy tax credits, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of: (1) 25 percent of net regular tax liability above $25,000 or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39).

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present-law credit for the manufacture of energy-efficient appliances.

Description of Proposal

The proposal would provide a credit for the production of certain energy-efficient clothes washers and refrigerators. The credit would equal $50 per appliance for energy-efficient clothes washers produced with a modified energy factor ("MEF") of 1.26 or greater and for refrigerators produced that consume 10 percent less kilowatt-hours per year than the energy conservation standards promulgated by the Department of Energy that took effect on July 1, 2001. The credit would equal $100 for energy-efficient clothes washers produced with a MEF of 1.42 or greater (1.5 or greater for washers produced after 2004) and for refrigerators produced that consume 15 percent less kilowatt-hours per year than the energy conservation standards promulgated by the Department of Energy that took effect on July 1, 2001. An energy-efficient refrigerator would be an automatic defrost refrigerator-freezer with an internal volume of at least 16.5 cubic feet to qualify for the credit. An energy-efficient clothes washer would be any residential clothes washer, including a residential style coin operated washer.

For each category of appliances (i.e., washers that meet the lower MEF standard, washers that meet the higher MEF standard, refrigerators that meet the 10 percent standard, refrigerators that meet the 15 percent standard), only production in excess of average production for each such category during calendar years 1999-2001 would be eligible for the credit. The taxpayer may not claim credits in excess of $30 million for all taxable years for appliances that qualify for the $50 credit, and may not claim credits in excess of $30 million for all taxable years for appliances that qualify for the $100 credit. Additionally, the credit allowed for all appliances may not exceed two percent of the average annual gross receipts of the taxpayer for the three taxable years preceding the taxable year in which the credit is determined. The present-law carry back rules of the general business credit generally would apply except that no credits attributable to energy-efficient appliances may be carried back before the effective date of this provision.

Effective Date

The credit would apply to appliances produced after December 31, 2002 and prior to (1) January 1, 2005 in the case of refrigerators that only meet the 10 percent credit standard, or (2) January 1, 2007 in the case of all other qualified energy-efficient appliances.

C. Tax Credit for Residential Fuel Cell, Solar and Wind Energy

Present Law

A nonrefundable, 10-percent business energy credit is allowed for the cost of new property that is equipment (1) that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat, or (2) used to produce, distribute, or use energy derived from a geothermal deposit, but only, in the case of electricity generated by geothermal power, up to the electric transmission stage.

The business energy tax credits are components of the general business credit (sec. 38(b)(1)). The business energy tax credits, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000 or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39).

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present-law personal tax credit for residential fuel cell, solar or wind energy property.

Description of Proposal

The proposal would provide a personal tax credit for the purchase of qualified wind energy property, qualified photovoltaic property, and qualified solar water heating property that is used exclusively for purposes other than heating swimming pools and hot tubs. The credit would be equal to 15 percent for solar water heating property and photovoltaic property, and would be equal to 30 percent for wind energy property. The maximum credit for each of these systems of property would be $2,000. The proposal would also provide a 30 percent credit for the purchase of qualified stationary or portable fuel cell power plants. The credit for any fuel cell may not exceed $1,000 for each kilowatt of capacity.

The credit would be nonrefundable and would be allowed against the regular and minimum tax. The depreciable basis of the property would be reduced by the amount of the credit.

Qualifying solar water heating property would mean an expenditure for property to heat water for use in a dwelling unit located in the United States and used as a residence if at least half of the energy used by such property for such purpose is derived from the sun. Qualified photovoltaic property would be property that uses solar energy to generate electricity for use in a dwelling unit. Solar panels would be treated as qualified photovoltaic property. Qualified wind energy property would be property that uses wind energy to generate electricity for use in a dwelling unit. A qualified fuel cell power plant is an integrated system comprised of a fuel cell stack assembly and associated balance of plant components that converts a fuel into electricity using electrochemical means, and which has an electricity-only generation efficiency of greater than 30 percent and generates at least 1 kilowatt of electricity using an electrochemical process. The qualified fuel cell power plant must be installed on or in connection with a dwelling unit located in the United States and used by the taxpayer as a principal residence. Expenditures for labor costs allocable to onsite preparation, assembly, or original installation of property eligible for the credit would be eligible expenditures.

Certain equipment safety requirements would need to be met to qualify for the credit. Special proration rules would apply in the case of jointly owned property, condominiums, and tenant-stockholders in cooperative housing corporations.

Effective Date

The credit would apply to purchases after December 31, 2002 and before January 1, 2008.

D. Business Tax Incentives for Fuel Cells

Present Law

A nonrefundable, 10-percent business energy credit is allowed for the cost of new property that is equipment (1) that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat, or (2) used to produce, distribute, or use energy derived from a geothermal deposit, but only, in the case of electricity generated by geothermal power, up to the electric transmission stage.

The business energy tax credits are components of the general business credit (sec. 38(b)(1)). The business energy tax credits, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000 or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39).

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present-law credit for fuel cell power plant property.

Description of Proposal

The proposal would provide a 30 percent credit for the purchase of qualified fuel cell power plants for businesses. A qualified fuel cell power plant is an integrated system comprised of a fuel cell stack assembly and associated balance of plant components that converts a fuel into electricity using electrochemical means, and which has an electricity-only generation efficiency of greater than 30 percent and which generates at least 1 kilowatt of electricity. The credit for any fuel cell may not exceed $1,000 for each kilowatt of capacity. The credit would be nonrefundable. The taxpayer's basis in the property would be reduced by the amount of the credit claimed.

Effective Date

The credit for businesses would apply to property placed in service after December 31, 2002 and before January 1, 2007, under rules similar to rules of section 48(m) of the Internal Revenue Code of 1986 (as in effect on the day before the date of enactment of the Revenue Reconciliation Act of 1990).

E. Allowance of Deduction for Energy-Efficient Commercial Building Property

Present Law

No special deduction is currently provided for expenses incurred for energy-efficient commercial building property.

Description of Proposal

The proposal would provide a deduction equal to energy-efficient commercial building property expenditures made by the taxpayer. Energy-efficient commercial building property expenditures would be amounts paid or incurred for energy-efficient commercial building property installed in connection with the new construction or reconstruction of property: (1) which would otherwise be depreciable property; (2) which is located in the United States, and (3) the construction or erection of which is completed by the taxpayer. The deduction would be limited to an amount equal to the product of $2.25 and the square footage of the property for which such expenditures were made. The deduction would be allowed in the year in which the property is placed in service.

Energy-efficient commercial building property would mean any property that reduces total annual energy and power costs with respect to the lighting, heating, cooling, ventilation, and hot water supply systems of the building by 50 percent or more in comparison to a reference building which meets the requirements of a Standard 90.1-1999 of the American Society of Heating, Refrigerating, and Air Conditioning Engineers and the Illuminating Engineering Society of North America. Certain certification requirements would have to be met.

For public property, such as schools, the Secretary would issue regulations to allow the deduction to be allocated to the person primarily responsible for designing the property in lieu of the public entity owner. Other rules would apply.

Effective Date

The proposal is effective for taxable years beginning after October 1, 2002 for plans certified prior to December 31, 2007, whose construction is completed on or before December 31, 2009.

F. Allowance of Deduction for Qualified Energy Management Devices and Retrofitted Qualified Meters

Present Law

No special deduction is currently provided for expenses incurred for qualified energy management devices.

Description of Proposal

The proposal would provide a $30 deduction for each qualified new or retrofitted energy management device placed in service by any taxpayer who is a supplier of electric energy or natural gas or is a provider of electric energy or natural gas services. A qualified energy management device would be any tangible property eligible for accelerated depreciation under section 168 and which is acquired and used by the taxpayer to enable consumers or others to manage their purchase, sale, or use of electricity in response to energy price and usage signals and which permits reading of energy price and usage signals on at least a daily basis.

The deduction would not be allowed to property used outside of the United States. The taxpayer would have basis reduction for such property equal to the deduction. Other rules would apply.

Effective Date

The proposal would be effective for any qualified energy management device placed in service after the date of enactment of the Act.

G. Three-Year Applicable Recovery Period for Depreciation of Qualified Energy Management Devices

Present Law

No special recovery period is currently provided for depreciation of qualified energy management devices.

Description of Proposal

The proposal would provide a 3-year recovery period for qualified new or retrofitted energy management devices placed in service by any taxpayer who is a supplier of electric energy or natural gas or is a provider of electric energy or natural gas services. A qualified energy management device would be any tangible property eligible for accelerated depreciation under code section 168 and which is acquired and used by the taxpayer to enable consumers or others to manage their purchase, sale, or use of electricity in response to energy price and usage signals and which permits reading of energy price and usage signals on at least a daily basis.

Effective Date

The proposal would be effective for any qualified energy management device placed in service after the date of enactment of the Act.

H. Energy Credit for Combined Heat and Power System Property

Present Law

A nonrefundable, 10-percent business energy credit is allowed for the cost of new property that is equipment (1) that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat, or (2) used to produce, distribute, or use energy derived from a geothermal deposit, but only, in the case of electricity generated by geothermal power, up to the electric transmission stage.

The business energy tax credits are components of the general business credit (sec. 38(b)(1)). The business energy tax credits, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000 or (2) the tentative minimum tax. For credits arising in taxable years beginning after December 31, 1997, an unused general business credit generally may be carried back one year and carried forward 20 years (sec. 39).

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present-law credit for combined heat and power ("CHP") property.

Description of Proposal

The proposal would provide a 10 percent credit for the purchase of combined heat and power property.

CHP property would mean property: (1) which uses the same energy source for the simultaneous or sequential generation of electrical power, mechanical shaft power, or both, in combination with the generation of steam or other forms of useful thermal energy (including heating and cooling applications); (2) which has an electrical capacity of more than 50 kilowatts or a mechanical energy capacity of more than 67 horsepower or an equivalent combination of electrical and mechanical energy capacities; (3) which produces at least 20 percent of its total useful energy in the form of thermal energy and at least 20 percent in the form of electrical or mechanical power (or a combination thereof); and (4) the energy efficiency percentage of which exceeds 60 percent (70 percent in the case of a system with an electrical capacity in excess of 50 megawatts or a mechanical energy capacity in excess of 67,000 horsepower, or an equivalent combination of electrical and mechanical capacities.)

CHP property would not include property used to transport the energy source to the generating facility or to distribute energy produced by the facility.

If a taxpayer is allowed a credit for CHP property, and the property would ordinarily have a depreciation class life of 15 years or less, the depreciation period for the property is treated as having a 22-year class life. The present-law carry back rules of the general business credit generally would apply except that no credits attributable to combined heat and power property may be carried back before the effective date of this provision.

Effective Date

The credit would apply to property placed in service after December 31, 2002 and before January 1, 2007.

IV. CLEAN COAL INCENTIVES

A. Investment and Production Credits for Clean Coal Technology

Present Law

Present law does not provide an investment credit for electricity generating facilities that use coal as a fuel. Nor does present law provide a production credit for electricity generated at facilities that use coal as a fuel. However, a nonrefundable, 10-percent investment tax credit ("business energy credit") is allowed for the cost of new property that is equipment (1) that uses solar energy to generate electricity, to heat or cool a structure, or to provide solar process heat, or (2) that is used to produce, distribute, or use energy derived from a geothermal deposit, but only, in the case of electricity generated by geothermal power, up to the electric transmission stage (sec. 48). Also, an income tax credit is allowed for the production of electricity from either qualified wind energy, qualified "closed-loop" biomass, or qualified poultry waste facilities placed in service prior to January 1, 2002 (sec. 45). The credit allowed equals 1.5 cents per kilowatt-hour of electricity sold. The 1.5 cent figure is indexed for inflation and equals 1.7 cents for 2001. The credit is allowable for production during the 10-year period after a facility is originally placed in service. The business energy tax credits and the production tax credit are components of the general business credit (sec. 38(b)(1)).

Description of Proposal

In general

The proposal would create three new credits: a production credit for electricity produced from qualifying clean coal technology units; a production credit for electricity produced from qualifying advanced clean coal technology; and a credit for investments in qualifying advanced clean coal technology facilities. Certain persons (public utilities, electric cooperatives, and the Tennessee Valley Authority) would be eligible to obtain certifications from the Secretary of the Treasury (as described below) for each of these credits and sell, trade, or assign the credit to any taxpayer.

Credit for investments in qualifying advanced clean coal technology facilities

The proposal would provide a 10-percent investment tax credit for qualified investments in advanced clean coal technology facilities. Qualifying advanced clean coal electricity production facilities must utilize advanced pulverized coal or atmospheric fluidized bed combustion technology, pressurized fluidized bed combustion technology, integrated gasification combined cycle technology, or some other technology certified by the Secretary of Energy. Any qualifying facility must meet certain capacity standards, thermal efficiency standards, and emissions standards for SO_2, nitrous oxides, particulate emissions, and source emissions standards as provided in the Clean Air Act. A qualifying advanced clean coal facility would not include any facility that uses "refined coal" (as defined Part V.J., of this document). In addition, the taxpayer would not be able to claim any investment credit with respect to a facility for which the taxpayer is not eligible to claim a production credit for electricity produced from any qualified advanced clean coal technology electricity generation unit as described below.

To be a qualified investment in advanced clean coal technology, the taxpayer must receive a certificate from the Secretary of the Treasury. The Secretary may grant certificates to investments only to the point that 4,000 megawatts of electricity production capacity qualifies for the credit. From the potential pool of 4,000 megawatts of capacity, not more than 1,000 megawatts in total and not more than 500 megawatts in years prior to 2009 shall be allocated to facilities using advanced pulverized coal or atmospheric fluidized bed combustion technology. From the potential pool of 4,000 megawatts of capacity, not more than 500 megawatts in total and not more than 250 megawatts in years prior to 2009 shall be allocated to facilities using pressurized fluidized bed combustion technology. From the potential pool of 4,000 megawatts of capacity, not more than 2,000 megawatts in total and not more than 1,000 megawatts in years prior to 2009 and not more than 1,500 megawatts in year prior to 2013 shall be allocated to facilities using integrated gasification combined cycle technology, with or without fuel or chemical co-production. From the potential pool of 4,000 megawatts of capacity, not more than 500 in total and not more than 250 megawatts in years prior to 2009 shall be allocated to any other technology for which a carbon emission rate is not more than 85 percent of conventional technology.

Production credit for electricity produced from qualifying clean coal technology units

The proposal provides a production credit for electricity produced from certain facilities that have been retrofitted, repowered, or replaced with a clean coal technology within ten years of the date of enactment. The value of the credit is 0.34 cents per kilowatt-hour of electricity produced and is indexed for inflation occurring after 2002 with the first potential adjustment in 2004. The taxpayer may claim the credit throughout the ten-year period commencing from the date on which the qualifying facility is placed in service.

A qualifying clean coal technology unit is a facility that meets certain capacity standards, thermal efficiency standards, and emissions standards for SO_2, nitrous oxides, particulate emissions, and source emissions standards as provided in the Clean Air Act. In addition, a qualifying clean coal technology unit would not be a facility that is receiving or is scheduled to receive funding under the Clean Coal Technology Program, the Power Plant Improvement Initiative, or the Clean Coal Power Initiative administered by the Secretary of the Department of Energy. Lastly, to be a qualified clean coal technology unit, the taxpayer must receive a certificate from the Secretary of the Treasury. The Secretary may grant certificates to facilities only to the point that 4,000 megawatts of electricity production capacity qualifies for the credit. However, no qualifying facility would be eligible if the facility's capacity exceeded 300 megawatts.

Production credit for electricity produced from qualifying advanced clean coal technology

The proposal also would provide a production credit for electricity produced from any qualified advanced clean coal technology electricity generation unit that qualifies for the investment credit for qualifying clean coal technology facilities, as described above. The production credit would be claimed on the sum of each kilowatt-hour of electricity produced and the heat value of other fuels or chemicals produced by the taxpayer at the facility.[2] The production credit would be claimed for the 10-year period commencing with the date the qualifying facility is placed in service. The value of the credit would vary depending upon the year the facility was placed in service, whether the facility produces solely electricity or electricity and fuels or chemicals, and the rated thermal efficiency of the facility. In addition, the value of the credit would be reduced for the second five years of eligible production. The value of the credit would be indexed for inflation occurring after 2002 with the first potential adjustment in 2004. The tables below specify the value of the credit (before indexing is applied).

Advanced clean coal technology facilities producing solely electricity

Facilities placed in service before 2009

The facility net heat rate, Btu/kWh adjusted for the heat content for the design coal is equal to:	Credit amount per kilowatt-hour	
	For the first five years	For the second five years
Not more than 8,400	\$.0060	\$.0038
More than 8,400 but not more than 8,550	\$.0025	\$.0010
More than 8,550 but less than 8,750	\$.0010	\$.0010

Facilities placed in service after 2008 and before 2013

The facility net heat rate, Btu/kWh adjusted for the heat content for the design coal is equal to:	Credit amount per kilowatt-hour	
	For the first five years	For the second five years
Not more than 7,770	\$.0105	\$.0090
More than 7,770 but not more than 8,125	\$.0085	\$.0068
More than 8,125 but less than 8,350	\$.0075	\$.0055

[2] Each 3,413 Btu of heat content of the fuel or chemical is treated as equivalent to one kilowatt-hour of electricity.

Facilities placed in service after 2012 and before 2017

The facility net heat rate, Btu/kWh adjusted for the heat content for the design coal is equal to:	Credit amount per kilowatt-hour	
	For the first five years	For the second five years
Not more than 7,380	$.0140	$.0115
More than 7,380 but not more than 7,720	$.0120	$.0090

Advanced clean coal technology facilities producing electricity and a fuel or chemical

Facilities placed in service before 2009

The facility design net thermal efficiency is equal to:	Credit amount per kilowatt-hour	
	For the first five years	For the second five years
Not less than 40.6%	$.0060	$.0038
Less than 40.6% but not less than 40%	$.0025	$.0010
Less than 40% but not less than 39%	$.0010	$.0010

Facilities placed in service after 2008 and before 2013

The facility design net thermal efficiency is equal to:	Credit amount per kilowatt-hour	
	For the first five years	For the second five years
Not less than 43.9%	$.0105	$.0090
Less than 43.9% but not less than 42%	$.0085	$.0068
Less than 42% but not less than 40.9%	$.0075	$.0055

Facilities placed in service after 2012 and before 2017

The facility design net thermal efficiency is equal to:	Credit amount per kilowatt-hour	
	For the first five years	For the second five years
Not less than 44.2%	$.0140	$.0115
Less than 44.2% but not less than 43.6%	$.0120	$.0090

Effective Date

The proposal relating to investment credits for advanced clean coal technology facilities would be effective after the date of enactment. The proposals relating to production credits would be effective after the date of enactment.

V. OIL AND GAS PROVISIONS

A. Tax Credit for Oil and Gas Production from Marginal Wells

Present Law

There is no credit for the production of oil and gas from marginal wells. The costs of such production may be recovered under the Code's depreciation and depletion rules and in other cases as a deduction for ordinary and necessary business expenses.

Description of Proposal

The proposal would create a new, $3 per barrel credit for the production of crude oil and a $0.50 credit per 1,000 cubic feet of qualified natural gas production. The maximum amount of production on which credit could be claimed would be 1,095 barrels or barrel equivalents. In both cases, the credit would be available only for production from a "qualified marginal well." The credit would not be available to production occurring if the reference price of oil exceeded $18 ($2.00 for natural gas). The credit would be reduced proportionately as for reference prices between $15 and $18 ($1.67 and $2.00 for natural gas). Reference prices would be determined on a one-year look-back basis.

A qualified marginal well would be defined as (1) a well production from which was marginal production for purposes of the Code percentage depletion rules or (2) a well that during the taxable year had (a) average daily production of not more than 25 barrel equivalents and (b) produced water at a rate of not less than 95 percent of total well effluent.

The credit would be treated as a general business credit.

Effective Date

The proposal would be effective for production in taxable years beginning after the date of enactment.

B. Natural Gas Gathering Lines Treated as Seven-Year Property

Present Law

The applicable recovery period for assets placed in service under the Modified Accelerated Cost Recovery System is based on the "class life of the property." The class lives of assets placed in service after 1986 are generally set forth in Revenue Procedure 87-56.[3] Revenue Procedure 87-56 includes two asset classes that could describe natural gas gathering lines owned by nonproducers of natural gas. Asset class 46.0, describing pipeline transportation, provides a class life of 22 years and a recovery period of 15 years. Asset class 13.2, describing assets used in the exploration for and production of petroleum and natural gas deposits, provides a class life of 14 years and a depreciation recovery period of seven years. The uncertainty regarding the appropriate recovery period of natural gas gathering lines has resulted in litigation between taxpayers and the IRS. The 10th Circuit Court of Appeals held that natural gas gathering lines owned by nonproducers falls within the scope of Asset class 13.2 (i.e., 7-year recovery period).[4] More recently, the U.S. District Court for the Eastern District of Michigan, Southern Division, held that natural gas gathering lines owned by nonproducers falls within the scope of Asset class 46.0 (i.e., 15-year recovery period).[5]

Description of Proposal

The proposal would establish a statutory 7-year recovery period and a class life of 10 years for natural gas gathering lines. A natural gas gathering line would be defined to include any pipe, equipment, and appurtenance that is (1) determined to be a gathering line by the Federal Energy Regulatory Commission, or (2) used to deliver natural gas from the wellhead or a common point to the point at which such gas first reaches (a) a gas processing plant, (b) an interconnection with an interstate transmission line, (c) an interconnection with an intrastate transmission line, or (d) a direct interconnection with a local distribution company, a gas storage facility, or an industrial consumer.

Effective Date

The proposal would be effective for property placed in service after date of enactment.

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[3] 1987-2 C.B. 674 (as clarified and modified by Rev. Proc. 88-22, 1988-1 C.B. 785).

[4] *Duke Energy v. Commissioner*, 172 F.3d 1255 (10th Cir. 1999), *rev'g* 109 T.C. 416 (1997). See also *True v. United States*, 97-2 U.S. Tax Cas. (CCH) par. 50,946 (D. Wyo. 1997).

[5] *Saginaw Bay Pipeline Co. v. United States*, 124 F. Supp. 2d 465 (E.D. Mich. 2001).

C. Repeal of Requirement of Certain Approved Terminals to Offer Dyed Diesel or Kerosene for Nontaxable Purposes

Present and Prior Law

Excise taxes are imposed on highway motor fuels, including gasoline, diesel fuel, and kerosene, to finance the Highway Trust Fund programs. Subject to limited exceptions, these taxes are imposed on all such fuels when they are removed from registered pipeline or barge terminal facilities, with any tax-exemptions being accomplished by means of refunds to consumers of the fuel. One such exception allows removal of diesel fuel and kerosene without payment of tax if the fuel is destined for a nontaxable use (e.g., use as heating oil) and is indelibly dyed.

Terminal facilities are not permitted to receive and store non-tax-paid motor fuels unless they are registered with the Internal Revenue Service. Under present law, a prerequisite to registration is that if the terminal offers for sale diesel fuel, it must offer both dyed and undyed diesel fuel. Similarly, if the terminal offers for sale kerosene, it must offer both dyed and undyed kerosene. This "dyed-fuel mandate" was enacted in 1997, to be effective on July 1, 1998. Subsequently, the effective date was delayed until July 1, 2000 and delayed again through December 31, 2001.

Description of Proposal

The proposal would repeal the diesel fuel and kerosene-dyeing mandate.

Effective Date

The proposal would be effective on January 1, 2002.

D. Expensing of Capital Costs Incurred and Credit for Production in Complying with Environmental Protection Agency Sulfur Regulations

Present Law

Taxpayers generally may recover the costs of investments in refinery property through annual depreciation deductions. Present law does not provide a credit for the production of low-sulfur diesel fuel.

Description of Proposal

The proposal would permit small business refiners to claim an immediate deduction (i.e., expensing) for up to 75 percent of the costs paid or incurred for the purpose of complying with the Highway Diesel Fuel Sulfur Control Requirements of the Environmental Protection Agency.

In addition, the proposal would provide that a small business refiner may claim a credit equal to five cents per gallon for each gallon of low sulfur diesel fuel produced during the period beginning one year after the date of enactment and ending with the date that is one year after the date on which the taxpayer must comply with applicable EPA regulations for the refinery. The total production credit claimed by the taxpayer would be limited to 25 percent of the capital costs incurred to come into compliance with the EPA diesel fuel requirements. No deduction would be allowed to the taxpayer for expenses otherwise allowable as a deduction in an amount equal to the amount of production credit claimed during the taxable year.

For these purposes a small business refiner is a taxpayer who within the business of refining petroleum products employs not more than 1,500 employees directly in refining on business days during a taxable year in which the deduction or production credit is claimed and had an average daily refinery run not exceeding 155,000 barrels per day for the year prior to enactment.

For taxpayers with an average daily refinery run in the year prior to enactment in excess of 155,000 and not greater than 205,000 barrels per day, the proposal would permit otherwise qualifying small business refiners to claim an immediate deduction for a percentage of qualifying capital costs equal to 75 percent less the percentage points determined by the excess of the average daily refinery runs over 155,000 barrels per day divided by 50,000 barrels per day. In addition, for these taxpayers, the limitation on the total production credit that may be claimed is reduced proportionately.

In the case of a qualifying small business refiner that is owned by a cooperative, the cooperative would be allowed to elect to pass any production credits to patrons of the organization.

Effective Date

The proposal would be effective for expenses paid or incurred after the date of enactment.

E. Determination of Small Refiner Exception to Oil Depletion Deduction

Present Law

Present law classifies oil and gas producers as independent producers or integrated companies. The Code provides numerous special tax rules for operations by independent producers. One such rule allows independent producers to claim percentage depletion deductions rather than deducting the costs of their asset, a producing well, based on actual production from the well (i.e., cost depletion).

A producer is an independent producer only if its refining and retail operations are relatively small. For example, an independent producer may not have refining operations the runs from which exceed 50,000 barrels on any day in the taxable year during which independent producer status is claimed.

Description of Proposal

The proposal would change the refinery limitation on claiming independent producer status from a limit based on actual daily production to a limit based on average daily production for the taxable year. Accordingly, the average daily refinery run for the taxable year could not exceed 50,000 barrels. For this purpose, the taxpayer would calculate average daily refinery run by dividing total production for the taxable year by the total number of days in the taxable year.

Effective Date

The proposal would be effective for taxable years beginning after December 31, 2002.

F. Extension of Suspension of Taxable Income Limit With Respect to Marginal Production

Present Law

In general

Depletion, like depreciation, is a form of capital cost recovery. In both cases, the taxpayer is allowed a deduction in recognition of the fact that an asset--in the case of depletion for oil or gas interests, the mineral reserve itself--is being expended in order to produce income. Certain costs incurred prior to drilling an oil or gas property are recovered through the depletion deduction. These include costs of acquiring the lease or other interest in the property and geological and geophysical costs (in advance of actual drilling).

Depletion is available to any person having an economic interest in a producing property. An economic interest is possessed in every case in which the taxpayer has acquired by investment any interest in minerals in place, and secures, by any form of legal relationship, income derived from the extraction of the mineral, to which it must look for a return of its capital.[6] Thus, for example, both working interests and royalty interests in an oil- or gas-producing property constitute economic interests, thereby qualifying the interest holders for depletion deductions with respect to the property. A taxpayer who has no capital investment in the mineral deposit does not possess an economic interest merely because it possesses an economic or pecuniary advantage derived from production through a contractual relation.

Cost depletion

Two methods of depletion are currently allowable under the Internal Revenue Code (the "Code"): (1) the cost depletion method, and (2) the percentage depletion method (secs. 611-613). Under the cost depletion method, the taxpayer deducts that portion of the adjusted basis of the depletable property which is equal to the ratio of units sold from that property during the taxable year to the number of units remaining as of the end of taxable year plus the number of units sold during the taxable year. Thus, the amount recovered under cost depletion may never exceed the taxpayer's basis in the property.

Percentage depletion and related income limitations

The Code generally limits the percentage depletion method for oil and gas properties to independent producers and royalty owners.[7] Generally, under the percentage depletion method 15 percent of the taxpayer's gross income from an oil- or gas-producing property is allowed as a deduction in each taxable year (sec. 613A(c)). The amount deducted generally may not exceed 100 percent of the net income from that property in any year (the "net-income limitation") (sec. 613(a)). By contrast, for any other mineral qualifying for the percentage depletion deduction, such deduction may not exceed 50 percent of the taxpayer's taxable income from the depletable

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[6] Treas. Reg. sec. 1.611-1(b)(1).

[7] Sec. 613A.

property. A similar 50-percent net-income limitation applied to oil and gas properties for taxable years beginning before 1991. Section 11522(a) of the Omnibus Budget Reconciliation Act of 1990 prospectively changed the net-income limitation threshold to 100 percent only for oil and gas properties, effective for taxable years beginning after 1990. The 100-percent net-income limitation for marginal wells has been suspended for taxable years beginning after December 31, 1997, and before January 1, 2002.

Additionally, the percentage depletion deduction for all oil and gas properties may not exceed 65 percent of the taxpayer's overall taxable income (determined before such deduction and adjusted for certain loss carrybacks and trust distributions) (sec. 613A(d)(1)).[8] Because percentage depletion, unlike cost depletion, is computed without regard to the taxpayer's basis in the depletable property, cumulative depletion deductions may be greater than the amount expended by the taxpayer to acquire or develop the property.

A taxpayer is required to determine the depletion deduction for each oil or gas property under both the percentage depletion method (if the taxpayer is entitled to use this method) and the cost depletion method. If the cost depletion deduction is larger, the taxpayer must utilize that method for the taxable year in question (sec. 613(a)).

Limitation of oil and gas percentage depletion to independent producers and royalty owners

Generally, only independent producers and royalty owners (as contrasted to integrated oil companies) are allowed to claim percentage depletion. Percentage depletion for eligible taxpayers is allowed only with respect to up to 1,000 barrels of average daily production of domestic crude oil or an equivalent amount of domestic natural gas (sec. 613A(c)). For producers of both oil and natural gas, this limitation applies on a combined basis.

In addition to the independent producer and royalty owner exception, certain sales of natural gas under a fixed contract in effect on February 1, 1975, and certain natural gas from geopressured brine,[9] are eligible for percentage depletion, at rates of 22 percent and 10 percent, respectively. These exceptions apply without regard to the 1,000-barrel-per-day limitation and regardless of whether the producer is an independent producer or an integrated oil company.

Description of Proposal

The suspension of the 100-percent net-income limitation for marginal wells would be extended an additional five years, through taxable years beginning before January 1, 2007.

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[8] Amounts disallowed as a result of this rule may be carried forward and deducted in subsequent taxable years, subject to the 65-percent taxable income limitation for those years.

[9] This exception is limited to wells, the drilling of which began between September 30, 1978, and January 1, 1984.

Effective Date

The proposal would be effective on date of enactment for taxable years after December 31, 2001.

G. Amortization of Geological and Geophysical Expenditures

Present Law

In general

Geological and geophysical expenditures are costs incurred by a taxpayer for the purpose of obtaining and accumulating data that will serve as the basis for the acquisition and retention of mineral properties by taxpayers exploring for minerals. A key issue with respect to the tax treatment of such expenditures is whether or not they are capital in nature. Capital expenditures are not currently deductible as ordinary and necessary business expenses, but are allocated to the cost of the property.[10]

Courts have held that geological and geophysical costs are capital, and therefore are allocable to the cost of the property[11] acquired or retained.[12] The costs attributable to such exploration are allocable to the cost of the property acquired or retained. As described further below, IRS administrative rulings have provided further guidance regarding the definition and proper tax treatment of geological and geophysical costs.

Revenue Ruling 77-188

In Revenue Ruling 77-188[13] (hereinafter referred to as the "1977 ruling"), the IRS provided guidance regarding the proper tax treatment of geological and geophysical costs. The ruling describes a typical geological and geophysical exploration program as containing the following elements:

- It is customary in the search for mineral producing properties for a taxpayer to conduct an exploration program in one or more identifiable project areas. Each

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[10] Under section 263, capital expenditures are defined generally as any amount paid for new buildings or for permanent improvements or betterments made to increase the value of any property or estate. Treasury regulations define capital expenditures to include amounts paid or incurred (1) to add to the value, or substantially prolong the useful life, of property owned by the taxpayer or (2) to adapt property to a new or different use. Treas. Reg. sec. 1.263(a)-1(b).

[11] "Property" means an interest in a property as defined in section 614 of the Code, and includes an economic interest in a tract or parcel of land notwithstanding that a mineral deposit has not been established or proved at the time the costs are incurred.

[12] See, *e.g.*, *Schermerhorn Oil Corporation v. Commissioner*, 46 B.T.A. 151 (1942). By contrast, section 617 of the Code permits a taxpayer to elect to deduct certain expenditures incurred for the purpose of ascertaining the existence, location, extent, or quality of any deposit of ore or other mineral (but not oil and gas). These deductions are subject to recapture if the mine with respect to which the expenditures were incurred reaches the producing stage.

[13] 1977-1 C.B. 76.

project area encompasses a territory that the taxpayer determines can be explored advantageously in a single integrated operation. This determination is made after analyzing certain variables such as (1) the size and topography of the project area to be explored, (2) the existing information available with respect to the project area and nearby areas, and (3) the quantity of equipment, the number of personnel, and the amount of money available to conduct a reasonable exploration program over the project area.

- The taxpayer selects a specific project area from which geological and geophysical data are desired and conducts a reconnaissance-type survey utilizing various geological and geophysical exploration techniques. These techniques are designed to yield data that will afford a basis for identifying specific geological features with sufficient mineral potential to merit further exploration.

- Each separable, noncontiguous portion of the original project area in which such a specific geological feature is identified is a separate "area of interest." The original project area is subdivided into as many small projects as there are areas of interest located and identified within the original project area. If the circumstances permit a detailed exploratory survey to be conducted without an initial reconnaissance-type survey, the project area and the area of interest will be coextensive.

- The taxpayer seeks to further define the geological features identified by the prior reconnaissance-type surveys by additional, more detailed, exploratory surveys conducted with respect to each area of interest. For this purpose, the taxpayer engages in more intensive geological and geophysical exploration employing methods that are designed to yield sufficiently accurate sub-surface data to afford a basis for a decision to acquire or retain properties within or adjacent to a particular area of interest or to abandon the entire area of interest as unworthy of development by mine or well.

The 1977 ruling provides that if, on the basis of data obtained from the preliminary geological and geophysical exploration operations, only one area of interest is located and identified within the original project area, then the entire expenditure for those exploratory operations is to be allocated to that one area of interest and thus capitalized into the depletable basis of that area of interest. On the other hand, if two or more areas of interest are located and identified within the original project area, the entire expenditure for the exploratory operations is to be allocated equally among the various areas of interest.

If no areas of interest are located and identified by the taxpayer within the original project area, then the 1977 ruling states that the entire amount of the geological and geophysical costs related to the exploration is deductible as a loss under section 165. The loss is claimed in the taxable year in which that particular project area is abandoned as a potential source of mineral production.

A taxpayer may acquire or retain a property within or adjacent to an area of interest, based on data obtained from a detailed survey that does not relate exclusively to any discrete property within a particular area of interest. Generally, under the 1977 ruling, the taxpayer allocates the entire amount of geological and geophysical costs to the acquired or retained property as a capital cost under section 263(a). If more than one property is acquired, it is proper to determine the amount of the geological and geophysical costs allocable to each such property by allocating the entire amount of the costs among the properties on the basis of comparative acreage.

If, however, no property is acquired or retained within or adjacent to that area of interest, the entire amount of the geological and geophysical costs allocable to the area of interest is deductible as a loss under section 165 for the taxable year in which such area of interest is abandoned as a potential source of mineral production.

In 1983, the IRS issued Revenue Ruling 83-105,[14] which elaborates on the positions set forth in the 1977 ruling by setting forth seven factual situations and applying the principles of the 1977 ruling to those situations. In addition, Revenue Ruling 83-105 explains what constitutes "abandonment as a potential source of mineral production."

Description of Proposal

The proposal would allow geological and geophysical costs incurred in connection with oil and gas exploration in the United States to be amortized over two years.

Effective Date

The proposal would be effective for geological and geophysical costs paid or incurred in taxable years beginning after December 31, 2002. No inference is intended from the prospective effective date of this proposal as to the proper treatment of pre-effective date geological and geophysical costs.

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[14] 1983-2 C.B. 51.

H. Amortization of Delay Rental Payments

Present Law

Present law generally requires costs associated with inventory and property held for resale to be capitalized rather than currently deducted as they are incurred. (sec. 263). Oil and gas producers typically contract for mineral production in exchange for royalty payments. If mineral production is delayed, these contracts provide for "delay rental payments" as a condition of their extension. In proposed regulations issued in 2000, the Treasury Department took the position that the uniform capitalization rules of section 263A require delay rental payments to be capitalized.[15]

Description of Proposal

The proposal would allow delay rental payments incurred in connection with the development of oil or gas within the United States to be amortized over two years.

Effective Date

The proposal would apply to delay rental payments paid or incurred in taxable years beginning after December 31, 2002. No inference is intended from the prospective effective date of this proposal as to the proper treatment of pre-effective date delay rental payments.

[15] 65 Fed. Reg. 6090 (2000).

I. Study of Coal Bed Methane

Present Law

Certain fuels produced from "non-conventional sources" and sold to unrelated parties are eligible for an income tax credit equal to $3 (generally adjusted for inflation) per barrel or BTU oil barrel equivalent (sec. 29). Qualified fuels must be produced within the United States.

Qualified fuels include:

(1) oil produced from shale and tar sands;

(2) gas produced from geopressured brine, Devonian shale, coal seams, tight formations ("tight sands"), or biomass; and

(3) liquid, gaseous, or solid synthetic fuels produced from coal (including lignite).

In general, the credit is available only with respect to fuels produced from wells drilled or facilities placed in service after December 31, 1979, and before January 1, 1993. An exception extends the January 1, 1993 expiration date for facilities producing gas from biomass and synthetic fuel from coal if the facility producing the fuel is placed in service before July 1, 1998, pursuant to a binding contract entered into before January 1, 1997.

The credit may be claimed for qualified fuels produced and sold before January 1, 2003 (in the case of non-conventional sources subject to the January 1, 1993 expiration date) or January 1, 2008 (in the case of biomass gas and synthetic fuel facilities eligible for the extension period).

Description of Proposal

The proposal would direct the Secretary of the Treasury to undertake a study of effect sec. 29 has had on the production of coal bed methane. The Secretary's study would be made in conjunction with the study to be undertaken by the Secretary of the Interior on the effects of coal bed methane production on surface and water resources, as provided in section 608 of S. 1766. The study would estimate the total amount of credit claimed annually and in aggregate related to the production of coal bed methane since the enactment of sec. 29. The study would report the annual value of the credit allowable for coal bed methane compared to the average annual wellhead price of natural gas (per thousand cubic feet of natural gas). The study would estimate the incremental increase in production of coal bed methane that has resulted from the enactment of sec. 29. The study would estimate the cost to the Federal government, in terms of the net tax benefits claimed, per thousand cubic feet of incremental coal bed methane produced annually and in aggregate since the enactment of sec. 29.

Effective Date

The proposal would be effective on the date of enactment.

J. Refined Coal

Present Law

Certain fuels produced from "non-conventional sources" and sold to unrelated parties are eligible for an income tax credit equal to $3 (generally adjusted for inflation) per barrel or BTU oil barrel equivalent (sec. 29). Qualified fuels must be produced within the United States.

Qualified fuels include:

(1) oil produced from shale and tar sands;

(2) gas produced from geopressured brine, Devonian shale, coal seams, tight formations ("tight sands"), or biomass; and

(3) liquid, gaseous, or solid synthetic fuels produced from coal (including lignite).

In general, the credit is available only with respect to fuels produced from wells drilled or facilities placed in service after December 31, 1979, and before January 1, 1993. An exception extends the January 1, 1993 expiration date for facilities producing gas from biomass and synthetic fuel from coal if the facility producing the fuel is placed in service before July 1, 1998, pursuant to a binding contract entered into before January 1, 1997.

The credit may be claimed for qualified fuels produced and sold before January 1, 2003 (in the case of non-conventional sources subject to the January 1, 1993 expiration date) or January 1, 2008 (in the case of biomass gas and synthetic fuel facilities eligible for the extension period).

Description of Proposal

The proposal would permit taxpayers to claim credit on qualifying liquid, gaseous, or solid synthetic fuels produced from coal (including lignite) from facilities placed in service after date of enactment and before January 1, 2007. A qualifying fuel is a fuel that when burned emits 20 percent less SO_2 and nitrogen oxides than the burning of feedstock coal or comparable coal predominantly available in the marketplace as of January 1, 2002, and if the fuel sells at prices at least 50 percent greater than the prices of the feedstock coal or comparable coal. However, no fuel produced from an advanced clean coal facility (as defined in Part IV.A) would qualify as qualifying fuel. The amount of credit would be $3.00 per barrel equivalent. The credit would be allowed for fuel produced during the five-year period beginning on the date the facility is placed in service.

Effective Date

The proposal would be effective for fuel sold after the date of enactment.

K. Natural Gas Distribution Lines Treated as Fifteen-Year Property

Present Law

The applicable recovery period for assets placed in service under the Modified Accelerated Cost Recovery System is based on the "class life of the property." The class lives of assets placed in service after 1986 are generally set forth in Revenue Procedure 87-56.[16] Natural gas distribution pipelines are assigned a 20-year recovery period and a class life of 35 years.

Description of Proposal

The proposal would establish a statutory 15-year recovery period and a class life of 20 years for natural gas distribution lines.

Effective Date

The proposal would be effective for property placed in service after the date of enactment.

[16] 1987-2 C.B. 674 (as clarified and modified by Rev. Proc. 88-22, 1988-1 C.B. 785).

VI. PROVISIONS RELATING TO ELECTRIC INDUSTRY RESTRUCTURING

The ultimate structure of the electric service industry when the currently anticipated overall industry restructuring is completed remains highly speculative at the present time. For example, the extent to which transmission activities will be consolidated into regional transmission organizations and the structure of those organizations has not been resolved. In particular, representatives of the Federal Energy Regulatory Commission ("FERC") have stated that FERC is *encouraging* formation of separate regional transmission organizations, but is not *requiring* utilities to divest themselves fully of ownership of their transmission assets when the utilities participate in such arrangements. Further, the role of public power entities, including the extent to which and the circumstances under which these entities legally or economically may be required to participate in open access arrangements, is unresolved.

The proposal recognizes that it is not possible at the present time to design tax provisions that will address an as yet undefined legal and economic industry structures. The proposal would put in place a mechanism to ensure that up-to-date information on tax issues that arise from future developments is available to the Congress so that appropriate changes to the tax law can be considered on a timely basis.

Further, on January 18, 2001, the Treasury Department published temporary and proposed regulations to provide guidance to issuers of governmental bonds for electric output facilities ("the regulations"). The regulations provide significant interim relief for outstanding electric output facility bonds. Because of this interim relief and the aforementioned uncertainty regarding future industry structure, the proposal does not address issues related to issuance of tax-exempt bonds. The proposal does, however, address certain aspects of electric industry restructuring that are known at the present time and for which comparable interim regulatory relief has not been provided -- issues relating to certain transfers of nuclear decommissioning plants by investor-owned utilities ("IOUs") and certain transactions engaged in by rural electric cooperatives.

A. Ongoing Study and Reports With Regard to Tax Issues Resulting from Future Restructuring Decisions

The proposal would direct the Department of the Treasury (in consultation with FERC) to conduct an ongoing study of tax issues resulting from restructuring of the electric service industry. The Treasury would be directed to report to Congress at least annually, no later than December 31, on tax issues identified since its last report. The first report would be due no later than December 31, 2002. These annual reports would continue until such time as the industry restructuring activities contemplated under the legislation in conjunction with which the proposal is to be considered have been completed.

Among other issues, this ongoing study would be expected to focus on the effect of restructuring on IOU's and cooperatives (e.g., asset divestitures). In addition, the proposal anticipates that the Treasury Department as part of the analysis underlying its ongoing study would review the interim relief provided to certain tax-exempt bonds in the regulations described above. As current uncertainties regarding the electric service industry are resolved, the proposal anticipates that the Treasury would, in an expeditious manner, adopt regulatory provisions that are consistent with its current regulatory authority under the Code. Where changes in the private business use rules are determined to require legislation, the proposal anticipates that the Treasury would include recommendations on such changes in its annual reports to Congress.

B. Modification to Special Rules for Nuclear Decommissioning Costs

Present Law

Overview

Special rules dealing with nuclear decommissioning reserve funds were adopted by Congress in the Deficit Reduction Act of 1984 ("1984 Act"), when tax issues regarding the time value of money were addressed generally. Under general tax accounting rules, a deduction for accrual basis taxpayers is deferred until there is economic performance for the item for which the deduction is claimed. However, the 1984 Act contains an exception under which a taxpayer responsible for nuclear powerplant decommissioning may elect to deduct contributions made to a qualified nuclear decommissioning fund for future decommissioning costs. Taxpayers who do not elect this provision are subject to general tax accounting rules.

Qualified nuclear decommissioning fund

A qualified nuclear decommissioning fund (a "qualified fund") is a segregated fund established by a taxpayer that is used exclusively for the payment of decommissioning costs, taxes on fund income, management costs of the fund, and for making investments. The income of the fund is taxed at a reduced rate of 20 percent for taxable years beginning after December 31, 1995.[17]

Contributions to a qualified fund are deductible in the year made to the extent that these amounts were collected as part of the cost of service to ratepayers (the "cost of service requirement").[18] Funds withdrawn by the taxpayer to pay for decommissioning costs are included in the taxpayer's income, but the taxpayer also is entitled to a deduction for decommissioning costs as economic performance for such costs occurs.

Accumulations in a qualified fund are limited to the amount required to fund decommissioning costs of a nuclear powerplant for the period during which the qualified fund is in existence (generally post-1984 decommissioning costs of a nuclear powerplant). For this purpose, decommissioning costs are considered to accrue ratably over a nuclear powerplant's estimated useful life. In order to prevent accumulations of funds over the remaining life of a nuclear powerplant in excess of those required to pay future decommissioning costs of such nuclear powerplant and to ensure that contributions to a qualified fund are not deducted more

[17] As originally enacted in 1984, a qualified fund paid tax on its earnings at the top corporate rate and, as a result, there was no present-value tax benefit of making deductible contributions to a qualified fund. Also, as originally enacted, the funds in the trust could be invested only in certain low risk investments. Subsequent amendments to the provision have reduced the rate of tax on a qualified fund to 20 percent and removed the restrictions on the types of permitted investments that a qualified fund can make.

[18] Taxpayers are required to include in gross income customer charges for decommissioning costs (sec. 88).

rapidly than level funding (taking into account an appropriate discount rate), taxpayers must obtain a ruling from the IRS to establish the maximum annual contribution that may be made to a qualified fund (the "ruling amount"). In certain instances (e.g., change in estimates), a taxpayer is required to obtain a new ruling amount to reflect updated information.

A qualified fund may be transferred in connection with the sale, exchange or other transfer of the nuclear powerplant to which it relates. If the transferee is a regulated public utility and meets certain other requirements, the transfer will be treated as a nontaxable transaction. No gain or loss will be recognized on the transfer of the qualified fund and the transferee will take the transferor's basis in the fund.[19] The transferee is required to obtain a new ruling amount from the IRS or accept a discretionary determination by the IRS.[20]

Nonqualified nuclear decommissioning funds

Federal and State regulators may require utilities to set aside funds for nuclear decommissioning costs in excess of the amount allowed as a deductible contribution to a qualified fund. In addition, taxpayers may have set aside funds prior to the effective date of the qualified fund rules.[21] The treatment of amounts set aside for decommissioning costs prior to 1984 varies. Some taxpayers may have received no tax benefit while others may have deducted such amounts or excluded such amounts from income. Since 1984, taxpayers have been required to include in gross income customer charges for decommissioning costs (sec. 88), and a deduction has not been allowed for amounts set aside to pay for decommissioning costs except through the use of a qualified fund. Income earned in a nonqualified fund is taxable to the fund's owner as it is earned.

Description of Proposal

Repeal of cost of service requirement

The proposal would repeal the cost of service requirement for deductible contributions to a nuclear decommissioning fund. Thus, all taxpayers, including unregulated taxpayers, would be allowed a deduction for amounts contributed to a qualified fund.

Clarify treatment of transfers of qualified funds and deductibility of decommissioning costs

The proposal would clarify the Federal income tax treatment of the transfer of a qualified fund. No gain or loss would be recognized to the transferor or the transferee as a result of the transfer of a qualified fund in connection with the transfer of the power plant with respect to which such fund was established. In addition, the proposal would provide that all nuclear decommissioning costs are deductible when paid.

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[19] Treas. reg. sec. 1.468A-6.

[20] Treas. reg. sec. 1.468A-6(f).

[21] These funds are generally referred to as "nonqualified funds."

Effective Date

The proposal would be effective for taxable years beginning after December 31, 2002.

C. Treatment of Certain Income of Electric Cooperatives

Present Law

In general

Under present law, an entity must be operated on a cooperative basis in order to be treated as a cooperative for Federal income tax purposes. Although not defined by statute or regulation, the two principal criteria for determining whether an entity is operating on a cooperative basis are: (1) ownership of the cooperative by persons who patronize the cooperative; and (2) return of earnings to patrons in proportion to their patronage. The Internal Revenue Service requires that cooperatives must operate under the following principles: (1) subordination of capital to control over the cooperative undertaking and financial benefits from ownership; (2) democratic control by the members of the cooperative; (3) vesting in and allocation among the members of all excess of operating revenues over the expenses incurred to generate revenues in proportion to their participation in the cooperative (patronage); and (4) operation at cost (not operating for profit or below cost).[22]

In general, cooperative members are those who participate in the management of the cooperative and who share in patronage capital. As described below, income from the sale of electric energy by an electric cooperative may be member or non-member income to the cooperative, depending on the membership status of the purchaser. A municipal corporation may be a member or non-member of a cooperative.

For Federal income tax purposes, a cooperative generally computes its income as if it were a taxable corporation, with one exception--the cooperative may exclude from its taxable income distributions of patronage dividends. In general, patronage dividends are the profits of the cooperative that are rebated to its patrons pursuant to a pre-existing obligation of the cooperative to do so. The rebate must be made in some equitable fashion on the basis of the quantity or value of business done with the cooperative.

Except for tax-exempt farmers' cooperatives, cooperatives that are subject to the cooperative tax rules of subchapter T of the Code (sec. 1381, *et seq.*) are permitted a deduction for patronage dividends from their taxable income only to the extent of net income is derived from transactions with patrons who are members of the cooperative (sec. 1382). The availability of such deductions from net income has the effect of allowing the cooperative to be treated like a conduit with respect to profits derived from transactions with patrons who are members of the cooperative.

Cooperatives that qualify as tax-exempt farmers' cooperatives are permitted to exclude patronage dividends from their taxable income to the extent of all net income, including net income derived from transactions with patrons who are not members of the cooperative,

[22] Announcement 96-24, Proposed Examination Guidelines Regarding Rural Electric Cooperatives, 1996-16 I.R.B. 35.

provided the value of transactions with patrons who are not members of the cooperative does not exceed the value of transaction with patrons who are members of the cooperative (sec. 521).

Taxation of electric cooperatives exempt from subchapter T

In general, the cooperative tax rules of subchapter T apply to any corporation operating on a cooperative basis (except mutual savings banks, insurance companies, other tax-exempt organizations, and certain utilities), including tax-exempt farmers' cooperatives (described in sec. 521(b)). However, subchapter T does not apply to an organization that is "engaged in furnishing electric energy, or providing telephone service, to persons in rural areas" (sec. 1381(a)(2)(C)). Instead, electric cooperatives are taxed under rules that were generally applicable to cooperatives prior to the enactment of subchapter T in 1962. Under these rules, an electric cooperative can exclude patronage dividends from taxable income to the extent of all net income of the cooperative, including net income derived from transactions with patrons who are not members of the cooperative.[23]

Tax exemption of rural electric cooperatives

Section 501(c)(12) provides an income tax exemption for rural electric cooperatives if at least 85 percent of the cooperative's income consists of amounts collected from members for the sole purpose of meeting losses and expenses of providing service to its members. The Internal Revenue Service takes the position that rural electric cooperatives also must comply with the fundamental cooperative principles described above in order to qualify for tax exemption under section 501(c)(12).[24] The 85-percent test is determined without taking into account any income from qualified pole rentals and cancellation of indebtedness income from the prepayment of a loan under sections 306A, 306B, or 311 of the Rural Electrification Act of 1936 (as in effect on January 1, 1987). The exclusion for cancellation of indebtedness income applies to such income arising in 1987, 1988, or 1989 on debt that either originated with, or is guaranteed by, the Federal Government. Rural electric cooperatives generally are subject to the tax on unrelated trade or business income under Code section 511.

Description of Proposal

Treatment of income from open access transactions

The proposal would provide that income received or accrued by a rural electric cooperative from any "open access transaction" (other than income received or accrued directly or indirectly from a member of the cooperative) is excluded in determining whether a rural electric cooperative satisfies the 85-percent test for tax exemption under section 501(c)(12). The term "open access transaction" is defined as any activity that would be a "permitted open access activity".

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[23] *See* Rev. Rul. 83-135, 1983-2 C.B. 149.

[24] Rev. Rul. 72-36, 1972-1 C.B. 151.

As applied to rural electric cooperatives, the term "permitted open access activity" is defined as--

(1) the provision or sale of transmission services or ancillary services on a nondiscriminatory open access basis: (i) pursuant to an open access transmission tariff filed with and approved by the Federal Energy Regulatory Commission ("FERC") (including acceptable reciprocity tariffs), but only if (in the case of a voluntarily filed tariff) the cooperative files a report with FERC within 90 days of enactment of this provision relating to whether or not the cooperative will join a regional transmission organization ("RTO"); or (ii) under an RTO agreement approved by FERC (including an agreement providing for the transfer of control--but not ownership--of transmission facilities);[25]

(2) the provision or sale of electric energy distribution services or ancillary services on a nondiscriminatory open access basis to end-users served by distribution facilities owned by the cooperative or its members;

(3) the delivery or sale of electric energy on a nondiscriminatory open access basis, provided that such electric energy is generated by a generation facility that is directly connected to distribution facilities owned by the cooperative (or its members) which owns the generation facility.

For purposes of the 85-percent test, the proposal also would provide that income received or accrued by a rural electric cooperative from any "open access transaction" is treated as an amount collected from members for the sole purpose of meeting losses and expenses, for purposes of the 85-percent test, if the income is received or accrued indirectly from a member of the cooperative.

<u>Treatment of income from nuclear decommissioning transactions</u>

The proposal would provide that income received or accrued by a rural electric cooperative from any "nuclear decommissioning transaction" also is excluded in determining whether a rural electric cooperative satisfies the 85-percent test for tax exemption under section 501(c)(12). The term "nuclear decommissioning transaction" is defined as--

(1) any transfer into a trust, fund, or instrument established to pay any nuclear decommissioning costs if the transfer is in connection with the transfer of the cooperative's interest in a nuclear powerplant or nuclear powerplant unit;

(2) any distribution from a trust, fund, or instrument established to pay any nuclear decommissioning costs; or

(3) any earnings from a trust, fund, or instrument established to pay any nuclear decommissioning costs.

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[25] Under this provision, references to FERC would be treated as including references to the Public Utility Commission of Texas or the Rural Utilities Service.

Treatment of income from asset exchange or conversion transactions

The proposal would provide that gain realized by a tax-exempt rural electric cooperative from a voluntary exchange or involuntary conversion of certain property is excluded in determining whether a rural electric cooperative satisfies the 85-percent test for tax exemption under section 501(c)(12). This provision only applies to the extent that: (1) the gain qualifies for deferred recognition under section 1031 (relating to exchanges of property held for productive use or investment) or section 1033 (relating to involuntary conversions); and (2) the replacement property that is acquired by the cooperative pursuant to section 1031 or section 1033 (as the case may be) constitutes property that is used, or to be used, either for the purpose of generating, transmitting, distributing, or selling electricity, or for the purpose of producing, transmitting, distributing, or selling natural gas.

Treatment of cancellation of indebtedness income from prepayment of certain loans

The proposal would provide that income from the prepayment of any loan, debt, or obligation of a tax-exempt rural electric cooperative that is originated, insured, or guaranteed by the Federal Government under the Rural Electrification Act of 1936 is excluded in determining whether the cooperative satisfies the 85-percent test for tax exemption under section 501(c)(12).

Treatment of income from load loss transactions

Tax-exempt rural electric cooperatives--The proposal would provide that income received or accrued by a tax-exempt rural electric cooperative from a "load loss transaction" is treated under 501(c)(12) as income collected from members for the sole purpose of meeting losses and expenses of providing service to its members. Therefore, income from load loss transactions would be treated as member income in determining whether a rural electric cooperative satisfies the 85-percent test for tax exemption under section 501(c)(12). The proposal also would provide that income from load loss transactions does not cause a rural electric cooperative to fail to be treated for Federal income tax purposes as a mutual or cooperative company under the fundamental cooperative principles described above.

The term "load loss transaction" would be defined as any wholesale or retail sale of electric energy (other than to a member of the cooperative) to the extent that the aggregate amount of such sales during a seven-year period beginning with the "start-up year" does not exceed the reduction in the amount of sales of electric energy for each year of such period by the cooperative to members. The "start-up year" is defined as the first year: (1) that the cooperative offers nondiscriminatory open access; or (2) in which at least 10 percent of the cooperative's sales of electric energy are to patrons who are not members of the cooperative.

The proposal also would exclude income received or accrued by rural electric cooperatives from load loss transactions from the tax on unrelated trade or business income.

Taxable electric cooperatives--The proposal would provide that similar rules apply to the receipt or accrual of income from load loss transactions of taxable electric cooperatives. For example, income from a load loss transaction would be excludible from the taxable income of a taxable electric cooperative if the cooperative distributes such income pursuant to a pre-existing contract to distribute the income to a patron who is not a member of the cooperative.

Effective Date

The proposal would be effective for taxable years beginning after the date of enactment.

VII. EXTENSION OF TAX INCENTIVES FOR INDIAN RESERVATIONS

A. Extension of Accelerated Depreciation and Wage Credit Benefits on Indian Reservations

Present Law

Present law includes the following tax incentives for businesses located within Indian reservations.

Accelerated depreciation

With respect to certain property used in connection with the conduct of a trade or business within an Indian reservation, depreciation deductions under section 168(j) will be determined using the following recovery periods:

3-year property	2 years
5-year property	3 years
7-year property	4 years
10-year property	6 years
15-year property	9 years
20-year property	12 years
Nonresidential real property	22 years

"Qualified Indian reservation property" eligible for accelerated depreciation includes property which is (1) used by the taxpayer predominantly in the active conduct of a trade or business within an Indian reservation, (2) not used or located outside the reservation on a regular basis, (3) not acquired (directly or indirectly) by the taxpayer from a person who is related to the taxpayer (within the meaning of section 465(b)(3)(C)), and (4) described in the recovery-period table above. In addition, property is not "qualified Indian reservation property" if it is placed in service for purposes of conducting gaming activities. Certain "qualified infrastructure property" may be eligible for the accelerated depreciation even if located outside an Indian reservation, provided that the purpose of such property is to connect with qualified infrastructure property located within the reservation (e.g., roads, power lines, water systems, railroad spurs, and communications facilities).

The depreciation deduction allowed for regular tax purposes is also allowed for purposes of the alternative minimum tax. The accelerated depreciation for Indian reservations is available with respect to property placed in service on or after January 1, 1994, and before January 1, 2004.

Indian employment credit

In general, a credit against income tax liability is allowed to employers for the first $20,000 of qualified wages and qualified employee health insurance costs paid or incurred by the employer with respect to certain employees (sec. 45A). The credit is equal to 20 percent of the excess of eligible employee qualified wages and health insurance costs during the current year over the amount of such wages and costs incurred by the employer during 1993. The credit is an incremental credit, such that an employer's current-year qualified wages and qualified employee health insurance costs (up to $20,000 per employee) are eligible for the credit only to the extent that the sum of such costs exceeds the sum of comparable costs paid during 1993. No deduction is allowed for the portion of the wages equal to the amount of the credit.

Qualified wages means wages paid or incurred by an employer for services performed by a qualified employee. A qualified employee means any employee who is an enrolled member of an Indian tribe or the spouse of an enrolled member of an Indian tribe, who performs substantially all of the services within an Indian reservation, and whose principal place of abode while performing such services is on or near the reservation in which the services are performed. An employee will not be treated as a qualified employee for any taxable year of the employer if the total amount of wages paid or incurred by the employer with respect to such employee during the taxable year exceeds an amount determined at an annual rate of $30,000 (adjusted for inflation after 1993).

The wage credit is available for wages paid or incurred on or after January 1, 1994, in taxable years that begin before December 31, 2003.

Description of Proposal

Accelerated depreciation

The proposal would extend the accelerated depreciation incentive for two years (to property placed in service before January 1, 2006).

Indian employment credit

The proposal would extend the Indian employment credit incentive for two years (to taxable years beginning before January 1, 2006).

Effective Date

The proposal would be effective on the date of enactment.

JOINT COMMITTEE ON TAXATION
February 11, 2002
JCX-03-02

ESTIMATED REVENUE EFFECTS OF THE "ENERGY TAX INCENTIVES ACT OF 2002" SCHEDULED FOR MARKUP BY THE COMMITTEE ON FINANCE ON FEBRUARY 13, 2002

Fiscal Years 2002 - 2012

[Millions of Dollars]

Provision	Effective	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2002-07	2002-12
Renewable Energy - Extend and Modify the Section 45 Credit for Producing Electricity From Certain Sources (including tradable credits)	esfqfa DOE	-30	-133	-242	-335	-363	-372	-372	-366	-359	-344	-291	-1,474	-3,207
Alternative Vehicles and Fuel Incentives														
1. Modified CLEAR Act:														
a. Credits for purchase of alternative motor vehicles and modifications to credit for electric vehicles	1/1/03	---	-50	-206	-320	-351	-219	22	15	10	4	1	-1,145	-1,093
b. Credit for retail sale of alternative fuels (30 cents/gallon in 2003, 40 cents in 2004, and 50 cents in 2005 through 2006)	1/1/03	---	-44	-100	-169	-215	-90	-1	-1	-1	-1	[1]	-619	-624
c. Extension of deduction for certain vehicles and refueling property	1/1/03	---	-50	-122	-133	-62	50	73	48	29	12	3	-316	-150
d. Credit for installation of alternative fueling stations	1/1/03	---	-2	-2	-2	-2	[1]	[2]	[2]	[2]	[2]	---	-9	-8
2. Modifications to small producer ethanol credit	tyba DOE	---	-16	-34	-34	-34	-34	-18	[1]	[1]	[1]	---	-152	-171
3. Transfer full amount of excise tax imposed on gasohol to the Highway Trust Fund	10/1/03	---------- No Revenue Effect ----------												
4. Modify income tax and fuels excise tax treatment of ETBE	DOE	---------- Negligible Revenue Effect ----------												
Total of Alternative Vehicles and Fuel Incentives		**---**	**-162**	**-464**	**-658**	**-664**	**-293**	**76**	**62**	**38**	**15**	**4**	**-2,241**	**-2,046**
Conservation and Energy Efficiency Provisions														
1. Business credit for construction of new energy efficient homes	DOE & ppisb 1/1/08	-8	-16	-16	-11	-8	-7	-4	-1	[1]	---	---	-66	-72
2. Tax credit for energy efficient appliances	tyea 12/31/02 & ppb 1/1/07	---	-19	-31	-33	-65	-50	-28	-13	-2	---	---	-198	-241
3. Tax credit for residential fuel cell, solar, and wind energy property	tyea 12/31/02 & ppb 1/1/08	---	-4	-18	-22	-29	-32	-30	---	---	---	---	-105	-135
4. Business tax incentives for qualifying fuel cells (through 12/31/06):														
a. Stationary	ppisa 12/31/02	---	-3	-8	-14	-16	-10	-6	-3	-2	[1]	---	-51	-62
b. Portable	ppisa 12/31/02	---------- Negligible Revenue Effect ----------												
5. Allowance of deduction for certain energy efficient commercial building property	pcpt 1/1/08 & 10/1/02 & ccb 1/1/10	---	-60	-61	-63	-64	-65	-65	-23	---	---	---	-313	-401
6. Allowance of deduction for new and retrofitted energy management devices; three-year applicable recovery period for depreciation of qualified new energy management devices	ppisa DOE	-11	-17	-20	-23	-24	-22	-20	-18	-17	-16	-16	-117	-205

Provision	Effective	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2002-07	2002-12
7. Energy credit for combined heat and power system property	episa 12/31/02 & episb 1/1/07	---	-34	-65	-72	-76	-51	-26	-15	-7	-1	---	-298	-347
Total of Conservation and Energy Efficiency Provisions		**-19**	**-153**	**-219**	**-238**	**-282**	**-237**	**-179**	**-73**	**-28**	**-17**	**-16**	**-1,148**	**-1,463**
Clean Coal Incentives - Investment and Production Credits for Clean Coal Technology														
1. Credit for production from a qualifying clean coal technology unit	pa DOE	---	-2	-33	-61	-73	-84	-91	-94	-97	-99	-101	-253	-733
2. Credit for investment in qualifying advanced clean coal technology	ppisa DOE	---	-1	-22	-54	-56	-47	-31	-77	-62	-26	-17	-180	-394
3. Credit for production from qualifying advanced clean coal technology	pa DOE	---	[1]	-5	-19	-42	-63	-80	-104	-136	-158	-171	-129	-780
Total of Clean Coal Incentives - Investment and Production Credit for Clean Coal Technology		**---**	**-3**	**-60**	**-134**	**-171**	**-194**	**-202**	**-275**	**-295**	**-283**	**-289**	**-562**	**-1,907**
Oil and Gas Provisions														
1. Tax credit for marginal domestic oil and natural gas well production	DOE	*No Revenue Effect*												
2. Natural gas gathering pipelines treated as 7-year property	ppisa DOE	-1	-4	-5	-6	-7	-8	-9	-11	-11	-12	-13	-31	-87
3. Repeal of requirement that certain terminals offer both dyed and undyed diesel fuel and kerosene as a condition of registration	DOE	*Negligible Revenue Effect*												
4. Expensing of capital costs incurred and credit for production in complying with Environmental Protection Agency sulfur regulations for small refiners	epoia DOE	---	---	---	---	-5	-10	-17	-27	-7	5	4	-14	-57
5. Determination of small refiner exception to oil depletion deduction - modify definition of independent refiner from daily maximum run less than 50,000 barrels to average daily run less than 50,000 barrels	tyba 12/31/02	---	-3	-5	-5	-6	-6	-6	-6	-6	-6	-7	-26	-57
6. Extension of suspension of 100% of taxable income limit with respect to marginal production (through 12/31/06)	tyba 12/31/01	-21	-35	-38	-40	-42	-15	---	---	---	---	---	-191	-191
7. Election to amortize geological and geophysical expenditures over 2 years (no transition rule)	cpoii tyba 12/31/02	---	291	205	-73	-154	-146	-146	-155	-161	-165	-170	122	-675
8. Election to amortize delay rental payments over 2 years (no transition rule)	apoii tyba 12/31/02	---	107	44	-82	-116	-116	-55	-86	-121	-123	-124	-162	-672
9. Study of coal bed methane	DOE	*No Revenue Effect*												
10. Refined coal ($3 credit and no indexing)	fsa DOE	---	[1]	-1	-4	-7	-8	-8	-7	-4	-1	---	-21	-41
11. Natural gas distribution lines treated as 15-year property	ppisa DOE	-8	-30	-59	-87	-111	-133	-152	-173	-199	-226	-254	-427	-1,431
Total of Oil and Gas Provisions		**-30**	**326**	**141**	**-297**	**-448**	**-442**	**-393**	**-465**	**-509**	**-528**	**-564**	**-750**	**-3,211**
Provisions Relating to Electric Industry Restructuring														
1. Ongoing study and reports with regard to tax issues resulting from future restructuring decisions	DOE	*No Revenue Effect*												

Provision	Effective	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2002-07	2002-12
2. Modification to Special Rules for Nuclear Decommissioning Costs - eliminate cost of service requirement and clarify treatment of fund transfers	tyba 2002	---	-18	-46	-56	-75	-99	-131	-143	-152	-161	-171	-294	-1,052
3. Treatment of certain income of electric cooperatives	tyba DOE	-6	-13	-16	-19	-21	-23	-25	-27	-29	-32	-35	-97	-245
Total of Provisions Relating to Electric Industry Restructuring		**-6**	**-31**	**-62**	**-75**	**-96**	**-122**	**-156**	**-170**	**-181**	**-193**	**-206**	**-391**	**-1,297**
Extension of Tax Incentives for Indian Reservations - Extension of Accelerated Depreciation and Wage Credit Benefits for Businesses on Indian Reservations (through 12/31/05)	**DOE**	**---**	**8**	**-153**	**-468**	**-427**	**-100**	**97**	**200**	**225**	**157**	**62**	**-1,140**	**-399**
NET TOTAL		**-85**	**-148**	**-1,059**	**-2,205**	**-2,451**	**-1,760**	**-1,129**	**-1,087**	**-1,109**	**-1,193**	**-1,300**	**-7,706**	**-13,530**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding.

Legend for "Effective" column:

apoii = amounts paid or incurred in
ccb = construction completed before
cpoii = costs paid or incurred in
DOE = date of enactment
epoia = expenses paid or incurred after
episa = equipments placed in service after
episb = equipment placed in service before
esfqfa = electricity sold from qualifying facilities after
fsa = fuels sold after
pa = production after
pcpt = plans certified prior to
ppb = property purchased before
ppisa = property placed in service after
ppisb = property placed in service before
tyba = taxable years beginning after
tyea = taxable years ending after

[1] Loss of less than $500,000.
[2] Gain of less than $500,000.

DESCRIPTION OF THE CHAIRMAN'S MODIFICATION TO THE "ENERGY TAX INCENTIVES ACT OF 2002"

Scheduled for Markup
By the
SENATE COMMITTEE ON FINANCE
on February 13, 2002

Prepared by
the Staff of the
JOINT COMMITTEE ON TAXATION

February 13, 2002
JCX-05-02

CONTENTS

INTRODUCTION

This document,[1] provides a description of the Chairman's Modification to the "Energy Tax Incentives Act of 2002," scheduled for a markup on February 13, 2002, by the Senate Committee on Finance.

[1] This document may be cited as follows: Joint Committee on Taxation, *Description of the Chairman's Modification to the Description of Chairman's Modification to the "Energy Tax Incentives Act of 2002"* (JCX-05-02), February 13, 2002.

I. MODIFICATIONS TO THE PROPOSALS IN THE CHAIRMAN'S MARK

A. Extension and Modification of the Section 45 Electricity Production Credit

The modification would add solar energy facilities as qualified facilities for purposes of claiming the electricity production credit under section 45. Qualifying solar energy facilities would be facilities using solar energy to generate electricity that are placed in service after the date of enactment and before January 1, 2007.

B. Modifications and Extensions of Provisions Relating to Electric Vehicles, Clean-Fuel Vehicles, and Clean-Fuel Vehicle Refueling Property

The effective date of proposal in the Chairman's Mark to modify and extend the present-law benefits for electric vehicles, to provide credits for qualified fuel cell motor vehicles, for qualified alternative fuel motor vehicles, and for qualified hybrid motor vehicles, to provide a credit for the installation of clean-fuel vehicle refueling property, and to provide a credit for the sale of alternative motor fuels would be accelerated to October 1, 2002. For heavy duty hybrid motor vehicles placed in service before 2003, the otherwise allowable credit ($1,000 to $10,000) is increased by between $3,500 and $14,000 depending upon the vehicle's weight and provided the vehicle meets certain 2007 (and beyond) emissions standards. The credit for the retail sale of qualifying alternative fuels would be 30 cents per gallon for qualifying sales in 2002.

In addition, the modification would clarify that qualifying alternative fuel motor vehicles are vehicles that operate only on qualifying alternative fuels and are incapable of operating on gasoline or diesel fuel (except to the extent gasoline or diesel fuel is part of a qualified mixed fuel).

C. Determination of Small Refiner Exception to Oil Depletion Allowance

The proposal in the Chairman's Mark to modify the operating limits on small refiners eligible for treatment as independent producers would be changed to specify a maximum operation level of 60,000 barrels of oil (rather than 50,000 barrels of oil).

D. Refined Coal

The proposal in the Chairman's Mark regarding refined coal would be modified to clarify that qualifying liquid, gaseous, or solid synthetic fuels produced from coal include fuels derived from high carbon fly ash.

E. Ongoing Study and Reports With Regard to Tax Issues Resulting from Future Electric Industry Restructuring Decisions

The proposal in the Chairman's Mark would be modified to clarify that, as part of the study, Treasury should exercise its authority, as appropriate, to modify or suspend regulations that may impede an electric utility company's ability to reorganize its capital stock structure to respond to a competitive marketplace.

II. ADDITIONAL PROVISIONS

A. Tax Credit for Certain Residential Energy Efficient Property

Present Law

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present-law personal tax credit for energy efficient residential property.

Description of Proposal

The proposal would provide a personal tax credit for the purchase of certain qualified energy efficient property:

Electric heat pump hot water heaters (equipment using electrically powered vapor compression cycles to extract heat from air and deliver it to a hot water storage tank) with an Energy Factor of at least 1.7 in the standard DOE test procedure. The maximum credit would be $75 per unit.

Electric heat pumps (equipment using electrically powered vapor compression cycles to extract heat from air in one space and deliver it to air in another space) with a heating efficiency of at least 9 HSPF (Heating Seasonal Performance Factor) and a cooling efficiency of at least 15 SEER (Seasonal Energy Efficiency Rating) and an energy efficiency ratio (EER) of 12.5 or greater. The maximum credit would be $250 per unit.

Geothermal heat pumps. With a SEER (Seasonal Energy Efficiency Rating) of at least 21. The maximum credit would be $250 per unit.

Natural gas heat pumps (equipment using either a gas-absorption cycle or a gas-driven engine to power the vapor compression cycle to extract heat from one source and deliver it to another) with a coefficient of performance for heating of at least 1.25 and for cooling of at least 0.70. The maximum credit would be $500 per unit.

Central air conditioners with an efficiency of at least 15 SEER and an EER of 12.5 or greater. The maximum credit would be $250 per unit.

Natural gas water heaters (equipment using a variety of mechanisms to increase steady-state efficiency and reduce standby and vent losses) with an Energy Factor of at least 0.8 in the standard Department of Energy (DOE) test procedure. The maximum credit would be $75 per unit.

The credits would be nonrefundable, and the depreciable basis of the property would be reduced by the amount of the credit. The credit would be allowed against the regular and minimum tax.

Effective Date

The credit would apply to purchases after December 31, 2002 and before January 1, 2008.

B. Credit for Energy Efficiency Improvements to Existing Homes

Present Law

A taxpayer may exclude from income the value of any subsidy provided by a public utility for the purchase or installation of an energy conservation measure. An energy conservation measure means any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit (sec. 136).

There is no present law credit for energy efficiency improvements to existing homes.

Description of Proposal

The proposal would provide a 10-percent nonrefundable credit for the purchase of qualified energy efficiency improvements. The maximum credit for a taxpayer with respect to the same dwelling for all taxable years is $300. A qualified energy efficiency improvement would be any energy efficiency building envelope component that is certified to meet or exceed the prescriptive criteria for such a component established by the 2000 International Energy Conservation Code, or any combination of energy efficiency measures that is certified to achieve at least a 30 percent reduction in heating and cooling energy usage for the dwelling and (1) that is installed in or on a dwelling located in the United States; (2) owned and used by the taxpayer as the taxpayer's principal residence; (3) the original use of which commences with the taxpayer; and (4) such component can reasonably be expected to remain in use for at least five years.

Building envelope components would be: (1) insulation materials or systems which are specifically and primarily designed to reduce the heat loss or gain for a dwelling; and (2) exterior windows (including skylights) and doors.

The taxpayer's basis in the property would be reduced by the amount of the credit. Special rules would apply in the case of condominiums and tenant-stockholders in cooperative housing corporations.

The credit would be allowed against the regular and minimum tax.

Effective Date

The credit would be effective for qualified energy efficiency improvements installed on or after the date of enactment and before January 1, 2006.

ESTIMATED REVENUE EFFECTS OF THE CHAIRMAN'S MODIFICATIONS TO THE "ENERGY TAX INCENTIVES ACT OF 2002," SCHEDULED FOR MARKUP BY THE COMMITTEE ON FINANCE ON FEBRUARY 13, 2002

Fiscal Years 2002 - 2012

[Millions of Dollars]

Provision	Effective	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2002-07	2002-12
Renewable Energy - Extend and Modify the Section 45 Credit for Producing Electricity From Certain Sources (including tradable credits)	esfqfa DOE	-30	-133	-242	-335	-363	-372	-372	-366	-359	-344	-291	-1,474	-3,207
Alternative Vehicles and Fuel Incentives														
1. Modified CLEAR Act:														
a. Credits for purchase of alternative motor vehicles and modifications to credit for electric vehicles	1/1/03	---	-50	-206	-320	-351	-219	22	15	10	4	1	-1,145	-1,093
b. Credit for retail sale of alternative fuels (30 cents/gallon in 2003, 40 cents in 2004, and 50 cents in 2005 through 2006)	1/1/03	---	-44	-100	-169	-215	-90	-1	-1	-1	-1	[1]	-619	-624
c. Extension of deduction for certain vehicles and refueling property	1/1/03	---	-50	-122	-133	-62	50	73	48	29	12	3	-316	-150
d. Credit for installation of alternative fueling stations	1/1/03	---	-2	-2	-2	-2	[1]	[2]	[2]	[2]	[2]	---	-9	-8
2. Modifications to small producer ethanol credit	tyba DOE	---	-16	-34	-34	-34	-34	-18	[1]	[1]	[1]	---	-152	-171
3. Transfer full amount of excise tax imposed on gasohol to the Highway Trust Fund	10/1/03	No Revenue Effect												
4. Modify income tax and fuels excise tax treatment of ETBE	DOE	Negligible Revenue Effect												
Total of Alternative Vehicles and Fuel Incentives		**---**	**-162**	**-464**	**-658**	**-664**	**-293**	**76**	**62**	**38**	**15**	**4**	**-2,241**	**-2,046**
Conservation and Energy Efficiency Provisions														
1. Business credit for construction of new energy efficient homes	DOE & ppisb 1/1/08	-8	-16	-16	-11	-8	-7	-4	-1	[1]	---	---	-66	-72
2. Tax credit for energy efficient appliances	tyea 12/31/02 & ppb 1/1/07	---	-19	-31	-33	-65	-50	-28	-13	-2	---	---	-198	-241
3. Tax credit for residential fuel cell, solar, and wind energy property	tyea 12/31/02 & ppb 1/1/08	---	-4	-18	-22	-29	-32	-30	---	---	---	---	-105	-135
4. Business tax incentives for qualifying fuel cells (through 12/31/06):														
a. Stationary	ppisa 12/31/02	---	-3	-8	-14	-16	-10	-6	-3	-2	[1]	---	-51	-62
b. Portable	ppisa 12/31/02	Negligible Revenue Effect												
5. Allowance of deduction for certain energy efficient commercial building property	pcpt 1/1/08 & 10/1/02 & ccb 1/1/10	---	-60	-61	-63	-64	-65	-65	-23	---	---	---	-313	-401
6. Allowance of deduction for new and retrofitted energy management devices; three-year applicable recovery period for depreciation of qualified new energy management devices	ppisa DOE	-11	-17	-20	-23	-24	-22	-20	-18	-17	-16	-16	-117	-205

Provision	Effective	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2002-07	2002-12
7. Energy credit for combined heat and power system property	episa 12/31/02 & episb 1/1/07	---	-34	-65	-72	-76	-51	-26	-15	-7	-1	---	-298	-347
Total of Conservation and Energy Efficiency Provisions		**-19**	**-153**	**-219**	**-238**	**-282**	**-237**	**-179**	**-73**	**-28**	**-17**	**-16**	**-1,148**	**-1,463**
Clean Coal Incentives - Investment and Production Credits for Clean Coal Technology														
1. Credit for production from a qualifying clean coal technology unit	pa DOE	---	-2	-33	-61	-73	-84	-91	-94	-97	-99	-101	-253	-733
2. Credit for investment in qualifying advanced clean coal technology	ppisa DOE	---	-1	-22	-54	-56	-47	-31	-77	-62	-26	-17	-180	-394
3. Credit for production from qualifying advanced clean coal technology	pa DOE	---	[1]	-5	-19	-42	-63	-80	-104	-136	-158	-171	-129	-780
Total of Clean Coal Incentives - Investment and Production Credit for Clean Coal Technology		**---**	**-3**	**-60**	**-134**	**-171**	**-194**	**-202**	**-275**	**-295**	**-283**	**-289**	**-562**	**-1,907**
Oil and Gas Provisions														
1. Tax credit for marginal domestic oil and natural gas well production	DOE	*No Revenue Effect*												
2. Natural gas gathering pipelines treated as 7-year property	ppisa DOE	-1	-4	-5	-6	-7	-8	-9	-11	-11	-12	-13	-31	-87
3. Repeal of requirement that certain terminals offer both dyed and undyed diesel fuel and kerosene as a condition of registration	DOE	*Negligible Revenue Effect*												
4. Expensing of capital costs incurred and credit for production in complying with Environmental Protection Agency sulfur regulations for small refiners	epoia DOE	---	---	---	---	-5	-10	-17	-27	-7	5	4	-14	-57
5. Determination of small refiner exception to oil depletion deduction - modify definition of independent refiner from daily maximum run less than 50,000 barrels to average daily run less than 50,000 barrels	tyba 12/31/02	---	-3	-5	-5	-6	-6	-6	-6	-6	-6	-7	-26	-57
6. Extension of suspension of 100% of taxable income limit with respect to marginal production (through 12/31/06)	tyba 12/31/01	-21	-35	-38	-40	-42	-15	---	---	---	---	---	-191	-191
7. Election to amortize geological and geophysical expenditures over 2 years (no transition rule)	cpoii tyba 12/31/02	---	291	205	-73	-154	-146	-146	-155	-161	-165	-170	122	-675
8. Election to amortize delay rental payments over 2 years (no transition rule)	apoii tyba 12/31/02	---	107	44	-82	-116	-116	-55	-86	-121	-123	-124	-162	-672
9. Study of coal bed methane	DOE	*No Revenue Effect*												
10. Refined coal ($3 credit and no indexing)	fsa DOE	---	[1]	-1	-4	-7	-8	-8	-7	-4	-1	---	-21	-41
11. Natural gas distribution lines treated as 15-year property	ppisa DOE	-8	-30	-59	-87	-111	-133	-152	-173	-199	-226	-254	-427	-1,431
Total of Oil and Gas Provisions		**-30**	**326**	**141**	**-297**	**-448**	**-442**	**-393**	**-465**	**-509**	**-528**	**-564**	**-750**	**-3,211**
Provisions Relating to Electric Industry Restructuring														
1. Ongoing study and reports with regard to tax issues resulting from future restructuring decisions	DOE	*No Revenue Effect*												

Provision	Effective	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2002-07	2002-12
2. Modification to Special Rules for Nuclear Decommissioning Costs - eliminate cost of service requirement and clarify treatment of fund transfers	tyba 2002	---	-18	-46	-56	-75	-99	-131	-143	-152	-161	-171	-294	-1,052
3. Treatment of certain income of electric cooperatives	tyba DOE	-6	-13	-16	-19	-21	-23	-25	-27	-29	-32	-35	-97	-245
Total of Provisions Relating to Electric Industry Restructuring		**-6**	**-31**	**-62**	**-75**	**-96**	**-122**	**-156**	**-170**	**-181**	**-193**	**-206**	**-391**	**-1,297**
Extension of Tax Incentives for Indian Reservations - Extension of Accelerated Depreciation and Wage Credit Benefits for Businesses on Indian Reservations (through 12/31/05)	**DOE**	**---**	**8**	**-153**	**-468**	**-427**	**-100**	**97**	**200**	**225**	**157**	**62**	**-1,140**	**-399**
The Chairman's Modifications														
1. Credit for energy efficient air conditioners, water heaters, heat pumps, and geothermal heat pumps	tyea 12/31/02	---	-21	-97	-55	-47	-38	-33	-34	-35	-36	-36	-259	-433
2. Credit for energy efficiency improvements to existing homes	tyeo/a DOE	---	-89	-117	-128	-111	-38	-10	---	---	---	---	-483	-494
3. Modify refined coal credit to include fly ash	fsa DOE	---	[1]	[1]	[1]	[1]	-1	-1	-1	[1]	[1]	---	-1	-3
4. Modified CLEAR Act - accelerate effective date	10/1/02	---	-19	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	-19	-20
5. Modify small refiners - 60,000 barrels average	tyba 12/31/02	---	-1	-1	-1	-1	-1	-1	-2	-2	-2	-2	-6	-14
6. Modify section 45 to add solar power	esfqfa DOE	[1]	[1]	[1]	[1]	[1]	-3	-7	-13	-11	-14	-15	-7	-65
7. Modify study on electricity restructuring	DOE	*No Revenue Effect*												
Total of the Chairman's Modifications		**[1]**	**-130**	**-215**	**-184**	**-159**	**-81**	**-52**	**-50**	**-48**	**-52**	**-53**	**-775**	**-1,029**
NET TOTAL		**-85**	**-278**	**-1,274**	**-2,389**	**-2,610**	**-1,841**	**-1,181**	**-1,137**	**-1,157**	**-1,245**	**-1,353**	**-8,481**	**-14,559**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding.

Legend for "Effective" column:
apoii = amounts paid or incurred in
ccb = construction completed before
cpoii = costs paid or incurred in
DOE = date of enactment
epoia = expenses paid or incurred after
episa = equipments placed in service after
episb = equipment placed in service before
esfqfa = electricity sold from qualifying facilities after
fsa = fuels sold after
pa = production after
pcpt = plans certified prior to
pfwda = produced from wells drilled after
ppb = property purchased before
ppisa = property placed in service after
ppisb = property placed in service before
tyba = taxable years beginning after
tyea = taxable years ending after
tyeo/a = taxable years ending on or after

[1] Loss of less than $500,000.
[2] Gain of less than $500,000.

February 13, 2002
1:00 pm

AMENDMENTS TO THE CHAIRMAN'S MARK
ENERGY TAX INCENTIVES ACT OF 2002
AMENDMENT SUMMARY

AMENDMENTS FILED IN SENATE FINANCE COMMITTEE		
NO.	**SENATOR**	**SUMMARY**
1	Rockefeller #1	Credit to capture coal mine methane (addition to section 45).
2	Rockefeller/ Hatch #2	Extend the section 29 credit for gas and oil obtained from non-conventional sources.
3	Rockefeller #3	Create a credit for clean coal waste recycling (under section 38).
4	Rockefeller #4	Under the energy efficiency section, add $75 credit for qualified energy efficient bottled/canned-beverage vending machines.
5	Breaux #1	Clarify the ability of municipal gas systems to use tax-exempt bonds to enter into pre-paid, long-term contracts for the purchase of natural gas.
6	Breaux #2	Section 29 – Permit a taxpayer to claim the section 29 credit for production of certain non-conventional fuels produced at wells drilled or facilities placed in service after the date of enactment and before the date that is 3 years after the date of enactment.
7	Breaux #3	Section 45 – allow for electricity produced from new black liquor (residual from wood pulping process) gasification to be eligible for the credit.
8	Breaux/ Thompson #1	Repeal (over the next 10 years) the excise tax on railroads and inland barges.
9	Conrad #1	Extend the expiration date of the credit for fuels produced/sold from non-conventional sources subject to the Jan. 1, 1993 expiration date (section 29) from Jan. 1, 2003 to Jan. 1, 2008.
10	Conrad/ Torricelli #1	Modify tax credit for qualified fuel cell power plants to include purchase of a stationary microturbine system.
11	Jeffords #1	Create a trust fund ("National Electric Systems Benefits Fund") to provide money for States to promote energy efficiency, renewable energy, low-income energy improvements, and support associated R&D.
12	Jeffords #2	Modify energy credit for combined heat and power system property
13	Bingaman #1	Electricity restructuring – private use rules for municipals and Transco relief for IOUs.
14	Bingaman #2	Extension and modification of credit for producing fuel from a non-conventional source
15	Bingaman #3	Provide credit for collection of coal mine methane.

Amendments Filed in Senate Finance Committee		
16	Bingaman #4	Provide tax credit to individual taxpayers for purchase of high-efficiency appliances and windows.
17	Bingaman #5	Renewable production tax credit – add solar energy as a qualifying energy resource (under section 45).
18	Bingaman #6	Modify tax credit to manufacturers of energy-efficient new homes.
19	Kerry #1	Provide tax credit to individual taxpayers for purchase of high-efficiency appliances and windows.
20	Kerry #2	Provide credit for high carbon fly ash (under section regarding Refined Coal).
21	Torricelli #1	Extend energy efficient credit for windows in existing homes (in addition to new homes).
22	Torricelli #2	Extend section 29 credit (for 5 years) to create tax incentives to produce fuels from non-conventional sources from new wells only.
23	Torricelli #3	Make municipal solid waste facilities eligible facilities under section 45.
24	Lincoln/ Grassley #1	Provide an income tax credit and excise tax rate reduction for biodiesel fuel mixtures.
25	Lincoln #2	Provide a tax credit for production of alternative fuels from agricultural and animal wastes.
26	Hatch/ Jeffords/ Kerry #1	Change the Chairman's mark for credits of new fuel cell vehicles, alternative motor fuels, hybrid motors and electric vehicles to be effective on enactment.
27	Hatch #1	Extend section 29 credit for production of non-conventional fuels produced at wells. Credit is $3.00 per barrel, capped at 200,000 cubic ft. or equivalent.
28	Murkowski #1	Provide a tax credit to provide a floor for natural gas produced on Alaska North Slope.
29	Nickles #1	Allow a utility to treat the sale of transmission assets to an independent transmission company as an involuntary conversion, and thereby allow the utility to defer capital gains tax as long as proceeds were invested in similar property within 4 years.
30	Nickles #2	Modify/reduce the section 45 electricity production credit amount.
31	Nickles #3	Section 45 electricity production credit – modify so only new facilities qualify for credit.
32	Nickles #4	Section 45 electricty production credit – strike "tradeable credits" language.
33	Gramm #1	Allow electric utilities an election to disregard nonparticipating preferred stock, within the meaning of section 1504(a)(4) for purposes of testing for "control" under section 368(c).

Amendments Filed in Senate Finance Committee		
34	Gramm #2	Strike the expansion of section 45 tax credits for renewable energy from bovine and swine waste.
35	Gramm #3	Strike the extension of section 45 tax credit for the burning of poultry waste for electricity.
36	Gramm #4	Strike the extension of section 45 tax credit for the burning of poultry waste for electricity, and strike the expansion of section 45 tax credits for renewable energy from bovine and swine waste.
37	Thompson #1	Provide a tax credit for the purchase of geothermal heat pumps for residential property.
38	Snowe/ Torricelli #1	Provide a 20% credit of the amount paid or incurred by a consumer for the installation of energy efficient windows on existing homes. Capped at $2,000.
39	Kyl #1	Alternative Minimum Tax ("Hold-Harmless" provision).
40	Kyl #2	Electric utility restructuring for municipals – allocation of private business use payments.
41	Kyl #3	Electric utility restructuring for municipals – treatment of modified output contracts.
42	Kyl #4	Transco relief.
43	Kyl #5	Extend section 45 tax credit without extending credit for electricity produced from poultry waste.
44	Kyl #6	Directs GAO to study and report on effectiveness of alternative vehicles and fuel incentives and the conservation and energy efficiency provisions.
45	Kyl #7	Strikes the alternative vehicles and fuel incentives provisions.
46	Kyl #8	Adds "Sense of the Senate" language that Congress should not raise taxes during the current economic recession.
47	Kyl #9	The repeal of the estate tax is made permanent (remove applicable sunset provision in EGTRRA)
48	Thomas #1	To exempt receipts for the construction of line extensions for new or potential customers from the "85-percent" member income test exemption The exemption would be available to tax-exempt rural electric cooperatives who receive Contribution in Aid of Construction (CAIC) payments to provide electricity service to coalbed methane well sites
49	Thomas #2	Modification to proposal on expensing of capital costs incurred and credit for production in complying with Environmental Protection Agency sulfur regulations.
50	Thomas/ Rockefellar #1	Extension and modification of credit for producing fuel from a non-conventional source (under section 29).

Date: 2/13/02 7:36 PM
Sender: Carla Martin
To: #All Staff (Dem-Rep); Brad Cannon; Richard Chriss; Carrie Clark; Hope Cooper; Faith Cristol; Kolan Davis; John Drake; Everett Eissenstat; Gina Falconio; Jill Gerber; John Gill; Diann Howland; Jill Kozeny; Ed McClellan; Tiffany McCullen; Christy Mistr; Elizabeth Paris; Mark Prater; Rebecca Reisinger; Steve Robinson; Colin Roskey; Leah Shimp; Ted Totman; Tom Walsh; Jason Wiley; Dean Zerbe; Alicia Ziemiecki
Priority: Normal
Subject: Results of Markup

The Chairman's Mark, entitled, The Energy Tax Incentives Act of 2002, was favorably reported by unanimous voice vote, as modified and amended.
The following amendments were offered:
Modification to Chairman's Mark, accepted without objection.
Amendment #50, Introduced by Senator Thomas, accepted without objection.
Amendment #24, Introduced by Senator Lincoln, passed by record vote:
    Ayes: Baucus, Rockefeller, Daschle (Proxy), Breaux, Conrad (Proxy), Graham, Jeffords,
    Bingaman, Kerry, Torricelli (Proxy), Lincoln, Grassley, Hatch, Murkowski, Thompson, Snowe,
    Nays: Nickles, Gramm, Lott, Kyl (Proxy), Thomas
Amendment #28, Introduced by Senator Murkowski, Withdrawn
Amendment #44, Introduced by Senator Baucus for Senator Kyl, was agreed to without objection, as modified by Senators Hatch and Nickles.