

T. Boone Pickens' decision to build a "Wind Farm" shows why the Wind Production Tax Credit (PTC) should NOT be extended

Right now, wind industry lobbyists are pushing the US Congress to extend the highly lucrative wind "Production Tax Credit" (PTC) – an action that could shift *another* \$3 billionⁱ in tax burden from "wind farm" owners to ordinary taxpayers.

A recent decision by Texas oil billionaire, T. Boon Pickens, reported by Reuters on April 18, 2008, shows why the Congress should end the wind Production Tax Credit.

According to the Reuters story,ⁱⁱ Pickens expects "...to turn at least a 25 per cent return" on his plan to spend \$10 billion to build the world's biggest "wind farm," consisting of 2,700 turbines and totaling 4,000 megawatts of generating capacity.

Mr. Pickens probably *can* make a 25% return by building a costly "wind farm" – but at the expense of millions of ordinary taxpayers and electric customers.

His decision shows dramatically what Congress and other federal and state officials have been slow to recognize; i.e., "*wind farms*" are being built primarily for their lucrative tax benefits and subsidies – not because of their environmental or energy benefits.

Contrary to wind advocates claims, "wind farms" are not environmentally benign, their environmental advantages are greatly overstated, and their adverse impacts are significant.

A 25% return with little risk.

Mr. Pickens' plan to earn a 25% return on a \$10 billion investment in wind may sound risky but with huge federal and state tax breaks and subsidies now available, there is little risk.

Detailed information -- e.g., on his financial and tax situation and plans for financing the venture -- would be needed to determine whether Mr. Pickens can achieve his expected 25% return.

However, calculations based on facts about *five* of the currently available federal and Texas tax breaks and subsidies show that his claim is realistic.

1. Wind Production Tax Credit (PTC). First, he would receive the Wind PTC, currently \$0.02 per kilowatt-hour (kWh) for electricity produced during the 1st 10 years of operation, which the Congress is being pressed to extend beyond its current December 31, 2008, expiration date. By itself, this tax credit would reduce his tax liability over 10 years by \$2.45 billion.ⁱⁱⁱ
2. Accelerated Depreciation. Second, his \$10 billion "wind farm" investment would qualify for the exceedingly generous 5-year, double declining balance accelerated depreciation for federal income tax purposes.^{iv} That means that the following amounts would be deducted from his otherwise taxable income and would further reduce his federal income tax liability; specifically:

Tax Year	Deduction from taxable income		Further reduction in income tax liability (in addition to PTC)
	% of Capital investment	Amount	
1 st	20%	\$2,000,000,000	\$ 700,000,000
2 nd	32%	\$3,200,000,000	\$1,120,000,000
3 rd	19.2%	\$1,920,000,000	\$ 672,000,000
4 th	11.52%	\$1,152,000,000	\$ 403,200,000
5 th	11.52%	\$1,152,000,000	\$ 403,200,000
6 th	5.76%	\$ 576,000,000	\$ 201,600,000
Totals	100%	\$10,000,000,000	\$3,500,000,000

Note that these deductions from otherwise taxable income and from tax liability could be taken regardless of whether the \$10 billion “wind farm” investment is financed with debt or equity.^v

Note also that, in addition to the further reduction in tax liability, this generous accelerated depreciation deduction for federal income tax purposes has two other huge benefits; specifically:

- a. Prompt recovery of all the owner’s equity investment. Quite likely, the equity investment would be no more than 50% with the remaining borrowed to reduce its cost. If Mr. Pickens provided equity of 50% (i.e., \$5 billion), the table above shows that he would recover thru depreciation deductions all of his equity investment in less than 2 years and in just over 1 year if the project begins operation late in the first tax year. With no remaining *equity* investment, his return on equity would be infinite.
- b. A large interest free loan. The depreciation deduction continues even though all equity has been recovered. Thus, Mr. Pickens would, in effect, be receiving an interest free loan, courtesy of US taxpayers for an amount equal to the debt financing.

If Mr. Pickens were unable to use all the tax deductions, schemes are available to “sell” the tax credits to other firms that have tax liabilities that they wish to avoid.

3. Texas franchise tax break. Tax breaks for “wind farms” are not limited to those provided by the federal government. Texas allows a corporation to deduct the cost of a “wind farm” from the Texas franchise tax in one of two ways: (1) the total cost of the system may be deducted from the company’s taxable capital; or, (2) 10% of the system’s cost may be deducted from the company’s income. Both taxable capital and a company’s income are taxed under the franchise tax, which is Texas’s equivalent to a corporate tax.^{vi} Details on Mr. Pickens financial and tax situation would be needed to estimate the value of this tax break.
4. Texas Renewable Portfolio Standard (RPS) and Renewable Energy Credits (RECs). In addition to all the tax breaks, Texas has virtually assured big profits for “wind farm” owners by requiring that a growing percentage of the electricity sold in Texas must come from “renewable” energy, which, in Texas is almost exclusively wind. The Texas’ RPS and REC schemes assure that revenue received by “wind farm” owners for their electricity and renewable energy credits will exceed normal market prices. The higher costs forced on electric distribution companies are passed along to electric customers in their monthly bills -- apparently with the blessing of the state’s political leaders and regulators.

5. Transmission Capacity – Another generous subsidy for Texas “wind farm” owners. Most of Texas’ “wind farms” are located distant from the areas where electricity is needed. Texas political leaders and regulators have mandated that additional transmission capacity will be built *and that the cost be borne by electric customers in their monthly bills*, not by the “wind farm” owners who are profiting so handsomely.^{vii} This requirement amounts to another huge subsidy for “wind farm” owners. Adding transmission capacity to serve distant “wind farms” is very costly. First, the estimated cost of building the transmission capacity ranges from \$3.78 billion to \$6.38 billion.^{viii} Second, significant amounts of electricity is lost as it moves over transmission lines, especially over long distances so not all the electricity that the “wind farm” produces ever reaches electric customers. Third, wind farms use transmission capacity inefficiently, resulting in high unit cost for the electricity that is eventually received.^{ix}

When all the tax breaks and subsidies are considered, Mr. Pickens’ 25% return on his investment looks very realistic.

Texas is not alone in making “wind farms” hugely profitable for owners and costly for taxpayers and electric customers. Various other states have adopted similar tax breaks and subsidies.

Those tax breaks and subsidies – adopted initially to help a “new” technology get a foothold in energy markets rapidly attracted a powerful industry constituency with millions of dollars to spend for lobbying, campaign contributions, and misleading advertising.

Harmful wealth transfers and misdirected capital investments.

For more than a decade, wind industry lobbyists and other wind energy advocates have *greatly overstated environmental and energy benefits of wind energy* and understated its adverse environmental, ecological, economic, scenic and property value impacts. Only during the last 3 years have the facts begun to emerge about the low quality and value of electricity from wind turbines, the high economic cost, and the adverse environmental, ecological, scenic and property value impacts.

Those facts are gradually making their way into the media but have yet to penetrate the US Congress and state governments. Instead, members of Congress and state officials parrot false and misleading claims from lobbyists and, even now, are proposing to extend huge, unwarranted tax benefits and subsidies for the industry.

These officials seem either not to recognize what they have done or not to care that federal and state wind energy policies, tax breaks and subsidies for the wind industry are:

- *Transferring hundreds of millions of dollars annually from the pockets of ordinary taxpayers and electric customers to a few large corporations that own “wind farms”-- or that buy tax credits from wind farm owners who cannot use them.* These include US firms such as the FPL Group that apparently has been able to escape paying *any* federal income tax in some years despite large profits, as well as several Wall Street and foreign-owned firms (e.g., Iberdrola, Shell, BP, Babcock & Brown) that wish to reduce the federal corporate income tax that they would otherwise have to pay on profits from other operations.

- *Misdirecting billions of capital investment dollars to energy projects (“wind farms”) that produce very little electricity – which electricity is low in quality and real value.* Electricity from wind turbines is intermittent, volatile, and unreliable. The electricity is low in real value because it is most likely to be produced at night in colder months, not on hot weekday late afternoons in July and August when electricity demand is highest. Further, because wind turbines are so unreliable, they cannot substitute for the *reliable* generating capacity required to meet growing electricity demand or replace old generating units.

Absent the huge tax breaks and subsidies for “wind farms,” billions in capital investment dollars could be available for more productive purposes.

Perhaps a recent analysis by the US Energy Information Administration (EIA) will begin to “get through to” members of Congress.^x That analysis shows that subsidies for wind energy in 2007 averaged over all the electricity produced by wind turbines in 2007 results in an astounding *federal* subsidy of more than 2.3 cents per kilowatt-hour.^{xi} EIA’s analysis did not include state subsidies.

Wind energy is a clear example of the great power of lobbyists and the lack of representation in Washington DC and state capitals for the interests of ordinary citizens, taxpayers and consumers.

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Endnotes:

ⁱ Joint Committee on Taxation analysis of H.R. 3221 as passed the Senate on April 10, 2008.
<http://www.house.gov/jct/x-33-08.pdf>

ⁱⁱ Chris Baltimore, Billionaire Texas oil man makes big bets on wind.
http://news.yahoo.com/s/nm/20080418/us_nm/usa_oil_pickens_wind_dc

ⁱⁱⁱ Assuming a 35% capacity factor, 4,000 MW of wind capacity would produce about 12,264,000,000 kWh of electricity per year or 122,640,000,000 kWh during the first 10 years of operation.

^{iv} Referred to by the IRS as Modified Accelerated Cost Recovery System (MACRS). See IRS Publication 946.

^v Note also that the US Congress, in the Economic Stimulus Act of 2008, added a 50% 1st year “bonus” deduction for 2008 investments. The effect of this additional “bonus” would permit “wind farm” owners to deduct 60% in the 1st, 16% in the 2nd, 9.6% in the 3rd, 5.76% in the 4th and 5th and 2.88% in the 6th tax years.

^{vi} Texas Statutes § 171.107; http://www.seco.cpa.state.tx.us/re_incentives-taxcode-statutes.htm#171107

^{vii} http://www.dsireusa.org/library/includes/incentive2.cfm?Incentive_Code=TX03R&state=TX&CurrentPageID=1&RE=1&EE=0

^{viii} http://www.ercot.com/meetings/board/keydocs/2008/B0415/Item_6_-_CREZ_Transmission_Report_to_PUC_-_Woodfin_Bojorquez.pdf

^{ix} Enough transmission capacity must be available to handle the full rated capacity of the wind farm but wind turbines produce electricity only when the wind blows in the right speed range (start producing around 6 mph, achieve rated capacity around 32 mph, cut out around 56 mph. Thus the output is intermittent, highly volatile and unreliable, with the turbines often producing less than rated capacity or not at all.

^x Wall Street Journal, May 12, 2007, p. A14; EIA, <http://www.eia.doe.gov/oiaf/servicerpt/subsidy2/index.html>

^{xi} EIA, <http://www.eia.doe.gov/oiaf/servicerpt/subsidy2/pdf/chap5.pdf>, Table 35, page 106.