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Legislative Text of Senate Tax Extenders (S. 1946, Tax Relief Extension Act of 2015): A Summary

Since passing a mark-up of tax extenders legislation in July – without actually publishing the text of the proposed statute – the Senate Finance Committee recently published the full text of S. 1946, the "Tax Relief Extension Act of 2015." As we have previously reported, this legislation includes reinstatement and amendment to the biodiesel and alternative fuel tax credits found in § 40A and § 6426.

Described by the accompanying Committee Report (S. Rep. 114-118), as seeking to encourage domestic production and increase American jobs, the legislation retroactively reinstates the biodiesel mixture income tax credit, the biodiesel fuel credit and the small biodiesel producer credit in § 40A and the biodiesel mixture excise tax credit in §§ 6426 and 6427(e) and extends the credits through December 31, 2016. However, effective January 1, 2016, both the income and excise tax credits become producer credits. This appears to depart from the Joint Committee on Taxation summary of the legislation which had suggested that only the § 40A income tax credit would become a producer credit. Under the proposal the existing credits will be converted to a $1.00 per gallon production credit for fuel produced in the United States. Unlike under current law where the credits are available for domestically produced and imported biodiesel (provided the imported biodiesel is not subsequently exported), the amended producer credit appears to limit the credit to only B100 that is produced in the United States; all imported B100 will not be eligible for the credit from 2016. This change may cause a significant reduction in imported B100 to be replaced with imported "bio-oils" which are then used to produce biodiesel in the United States. With respect to the § 40A income tax credit the small producer credit would remain, allowing small producers to claim an additional $0.10 per gallon credit on the first 15,000,000 gallons of biodiesel produced.

The amendment does allow an "eligible discretionary blender" – defined as "a diesel fuel blender registered with the IRS that blended 10 million of more gallons of biodiesel or renewable diesel in the previous calendar year" – to claim the mixture credit if the producer provides the blender with documentation that the producer is foregoing the production credit. This would allow the industry to continue to operate as it always has with respect to the credits; despite the apparent significant changes all the legislation really does is limit the credit to biodiesel produced in the United States.

In addition to modifying the tax credits, the legislation also brings biodiesel within the definition of taxable fuel, taxing it the same as petroleum diesel, treating biodiesel production and blending facilities as refineries and requiring both producers and the production and blending facilities to be properly registered with the IRS. With respect to registration it would seem that biodiesel production facilities as well as any production or terminal location where blending occurs will be required to become registered refineries while terminals storing biodiesel will need to be registered IRS terminals; it would also appear

that current EX-STARS reporting requirements for terminal operators (including biodiesel refineries that have a rack and are assigned a Terminal Control Number (TCN) will extend to biodiesel.

With respect to the tax, it is imposed on the first removal of biodiesel from the bulk terminal system which would seem to mean that biodiesel would be taxed when removed at the production facility and placed into a railcar which is the predominate mode of biodiesel transportation. This would mean the incidence of taxation would occur soon after production as there are no biodiesel pipelines to move biodiesel from production facility to terminals. However, possibly recognizing the economic burden this would place on biodiesel producers as well as the administrative burden placed on the IRS and taxpayers of dealing with first and second taxpayer reports, the legislation includes a special rule exempting from the tax "the removal or entry of biodiesel to any refinery or terminal if the person removing or entering the biodiesel and the operator of the refinery or terminal are registered under section 4101." In other words, provided the biodiesel producer and his customer are both registered, and the customer removes the biodiesel from a refinery to transport it to a registered terminal, the tax will not be imposed. The reality of this means that biodiesel, like diesel, will most often be taxed when it is removed from a terminal at the rack and not further up the supply chain.

Moreover, in the definitions section of the legislation, the tax credit and excise tax on biodiesel appear to be linked through a requirement that the person who pays the tax is the person who receives the tax credit. The legislation states that the tax credits are available to an "eligible taxpayer" and defines an "eligible taxpayer" as the producer of biodiesel if that producer has paid the biodiesel tax. The legislation goes on to state that an "eligible discretionary blender" shall be treated as the producer (and therefore as the "eligible taxpayer") where the producer has not paid the biodiesel tax, the producer assigns the right to the credit and the "eligible discretionary blender" pays the tax. When the historic operation of the industry is considered within the framework of the statute as a whole, this language would appear to tax biodiesel at the terminal rack and offer the credit only to blenders of motor vehicle suitable blends (*e.g.* B20). In other words, the rack blender will likely be the entity claiming the credit.

With respect to alternative fuel, the legislation extends both the alternative fuel and alternative fuel mixture credits through the end of 2016 retroactive to January 1, 2015. The conditions for claiming the credits are unchanged. However, with respect to Liquefied Natural Gas (LNG) and Liquefied Petroleum Gas (LPG) there is a change to the calculation of the credit. The recent extension of Highway Funding in the Surface Transportation Act of 2015 included a change to the excise tax on LNG and LPG. Effective January 1, 2016, this law changes the excise tax rate of LNG to a rate based on its energy equivalent of a gallon of diesel (DGE) and changes the excise tax rate of LPG to a rate based on its energy equivalent of a gallon of gasoline (GGE). The revised proposed tax rates are $0.243 per DGE for LNG (effectively $0.141per gallon) and $0.183 per GGE for LPG (effectively $0.132 per gallon). A conforming amendment is proposed for the $0.50 per gallon tax credits such that these would be determined on $0.50 per DGE for LNG (approximately $0.29 per gallon) and $0.50 GGE for LPG (approximately $0.36 per gallon). However, the legislative text states that all amendments to the alternative fuel and alternative fuel mixture credits are effective January 1, 2015 so it remains to be seen whether a further amendment will conform the energy equivalent conversions to the Surface Transportation Act.

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