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Incentives regarding the use of renewable energy can be designed in many different ways, and no preferred method seems to exist among the legislatures of the world. Taxation plays a material role as a climatic and environmental political tool. Basic tax law also influences the prevalence of renewable energy and clean technology.

This article contains information about a new bill in Denmark designed to improve the taxation regime regarding renewable energy for private individuals.

General Remarks

On September 17, 2010, the legislature adopted new rules regarding individuals' investment in renewable energy. The legislation is effective as of January 1, 2011.

The purpose of the new rules is to improve and simplify the conditions for individuals who invest in renewable energy plants (REPs). Thus, the intention of the new rules is to entice individuals to invest in REPs.

The Existing Rules

Energy produced by a REP that is not sold to the electricity grid is not liable for taxes or duties on the produced energy. The production of energy for personal use is not taxable, and expenses incurred in connection with constructing and operating the REP are not deductible.

Energy producers connected to the grid are generally subject to taxation on the income generated by the sale of energy, unless otherwise provided in the tax laws. Similarly, individuals who invest in REPs or in an equity interest in REPs must include the income derived from the REP in their taxable income.

The regulations regarding duties on electricity were amended in June 2010. According to these rules, electricity that a household produces on its own REP (for example, through a windmill or solar panel) is in some cases completely exempt from the regular duty on electricity. The REP is capable of storing excess electricity on the public grid for later use. Thus, the meter on the REP is capable of "running backwards." The favorable rules only apply to REPs of 6 kwh or less.

The tax aspects of the REP regime were addressed during the debate on the amendments to the law on duties on electricity. During this debate Minister of Taxation Troels Lund Poulsen said that all producers who sell electricity to the public grid are taxable on the income derived regardless of the source of the electricity. Accordingly, income from the sale of electricity to the grid is considered taxable.

Producers who do not sell electricity to the public grid are not taxed on the income related to the production of electricity. Also, producers that store electricity at the place of production, where the electricity is solely used for the producer's own use, are not taxed.

As a corollary, expenses incurred in connection with constructing and operating the REP are not deductible.

Under the rules existing before January 1, 2011, individuals who own windmills or equity interests in windmills could choose to be taxed according to a schematic arrangement under which only 60 percent of the gross income derived from the windmill that exceeded DKK 3,000 was taken into account in determining taxable income. The remaining 40 percent was tax free, so deductions were not allowed. If the taxpayer chose the schematic arrangement, the windmill or the equity interest in a windmill was considered to be exclusively of a noncommercial nature. If the taxpayer did not choose the schematic arrangement, the windmill was considered exclusively of a commercial nature.

The New Rules

The new rules significantly expand the existing rules' scope; all types of REPs are now included. The qualifying REPs are no longer limited to electricity producing plants, meaning that heat producing plants, for example, are also included. The new rules reference the law on the promotion of renewable energy, under which renewable energy includes wind power, biogas, biomass, solar power, tidal wave power, and geothermal heat. Also, the Minister of Climate and Energy can adopt rules on which types of energy qualify as renewable energy, thereby allowing for future, currently unknown types of energy to also qualify. (The existing rules apply only to windmills.)

The basic deduction under the new rules is increased from DKK 3,000 to DKK 7,000 in the schematic arrangement. Thus, only income derived from REPs that exceed DKK 7,000 is included from taxable income (marginal tax rate of approximately 55 percent).

The plants that fall within the scope of the proposed rules are limited to the following:

- REPs that solely produce energy for a single household.
- REPs or equity interests in REPs in which the plants or interest were acquired at cost — that is, at a price equal to the proportional share of the costs to the individual who constructed the plant. More specifically, the cost is determined in accordance with the same principles that apply to the option arrangement under section 14 of the law on the promotion of renewable energy.
- Windmills or equity interests in windmills in which income is taxed under the schematic arrangement.

With the adoption of the new rules, there may be windmills that are taxed according to the schematic arrangement that will not meet the requirements of the new rules (for example, if the initial purchase price does not meet the new cost price conditions). To prevent this outcome, the proposed rules will allow windmills or equity interests in windmills, which are using the current rules, to continue to do so throughout the useful life of the windmill, provided that the schematic arrangement was used by the owners during the 2009 tax year.

Under the new rules, no deductions, including depreciation deductions, are allowed for expenses connected with operating the REP if the schematic arrangement is used. This corresponds to the current rules applicable under the windmill schematic arrangement.

The rules on the schematic arrangement do not include any limitation on kilowatt-hour capacity. ◆