
State of South Carolina
Department of Revenue
Office of General Counsel
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SC PRIVATE LETTER RULING #11-6

SUBJECT: Availability of Biomass Energy Credits to Limited Liability Company
(Income Tax)

REFERENCES: S.C. Code Ann. Section 12-2-25 (Supp. 2010)
S.C. Code Ann. 12-6-30(1) (2000)
S.C. Code Ann. Section 12-6-3310 (2000, Supp. 2010)
S.C. Code Ann. Section 12-6-3620 (Supp. 2010)

AUTHORITY: S. C. Code Ann. Section 12-4-320 (2000)
S. C. Code Ann. Section 1-23-10(4) (2005)
SC Revenue Procedure #09-3

SCOPE: A Private Letter Ruling is an advisory opinion issued to a specific taxpayer by the Department to apply principles of law to a specific set of facts or a particular tax situation. It is the Department's opinion limited to the specific facts set forth, and is binding on agency personnel only with respect to the person to whom it was issued and only until superseded or modified by a change in statute, regulation, court decision, or another Departmental advisory opinion, providing the representations made in the request reflect an accurate statement of the material facts and the transaction was carried out as proposed.

Facts

ABC LLC ("ABC") is a limited liability company that is organized and domiciled in South Carolina. ABC will be in the business of identifying, designing, constructing, and managing biomass energy sites. ABC is a calendar year limited liability company that has chosen to be taxed as a partnership. ABC has two members, XYZ, Inc. ("Member A") and 123 LLC ("Member B"). Member A is a South Carolina incorporated and domiciled S Corporation that has four South Carolina resident individual shareholders.¹ Member A owns 60% of ABC. Member B is a North Carolina limited liability company with 3 members. Member B owns 40% of ABC. Member B is not a party to the ruling request and therefore, information about the ultimate ownership of Member B is not included in this discussion.

¹ For purposes of this ruling, it is assumed that Member A will not have any corporate level tax.

ABC is planning to install qualifying equipment that will be used to create heat, power, steam, electricity, or another form of energy for commercial use from a fuel consisting of no less than ninety percent qualifying biomass resource. ABC has also indicated that it may sell some of the energy created at an eligible site to a related party as well as to other non-related consumers. Up to \$10,000,000 dollars will be invested in biomass related equipment at a single site. This investment may occur over a single tax year or several tax years.

ABC has posed several questions about its qualification for the biomass credit contained in Code Section 12-6-3620. For purposes of this private letter ruling, it is presumed that ABC will meet all the requirements of the statute regarding the purchase and installation of eligible equipment and that the equipment will be producing the required heat, power, steam, electricity, or another form of energy for commercial use from a fuel consisting of no less than ninety percent qualifying biomass resource.

Law

Code Section 12-2-25 provides in relevant part:

- (A) As used in this title and in other titles which provide for taxes administered by the department and unless otherwise required by the context:
 - (1) “partnership” includes a limited liability company taxed for South Carolina income tax purposes as a partnership;
 - (2) “partner” includes a member of a limited liability company taxed for South Carolina income tax purposes as a partnership.
- ...

Code Section 12-6-30(1) provides in relevant part:

- “As used in this chapter, the following words have the meaning provided unless otherwise required by the context:
- (1) ‘Taxpayer’ includes an individual, trust, estate, partnership, association, company, corporation, or any other entity subject to the tax imposed by this chapter or required to file a return.”
- ...

Code Section 12-6-3310 provides in relevant part:

- (A) Credits allowed in this article are nonrefundable and may be used only in the year generated unless otherwise provided.
- (B)(1) Unless specifically prohibited, an “S” corporation, limited liability company taxed as a partnership, or partnership that qualifies for a credit pursuant to this article may pass through the credit earned to each shareholder of the “S” corporation, member of the limited liability company, or partner of the partnership.

(2) A credit earned by an “S” corporation owing corporate level income tax must first be used at the entity level. Only the remaining credit passes through to the shareholders of the “S” corporation.

(3) The amount of the credit allowed a shareholder, partner, or member is equal to the percentage of the shareholder’s stock ownership, partner’s interest in the partnership, or member’s interest in the limited liability company for the taxable year multiplied by the amount of the credit earned by the entity and available for pass through. Limitations upon reduction of income tax liability by use of a credit are computed based on the shareholder’s, partner’s, or member’s tax liability. The credit is allowed against the type of tax or taxes specifically provided by the credit in this article.

(C) A limited liability company not organized as a legal entity which is a taxpayer, a corporation, or other form of business entity expressly specified as qualifying for the credits allowed pursuant to this article nevertheless qualifies for such credits in a manner consistent with Section 12-2-25 as follows:

(1) Limited liability companies taxed for South Carolina income tax purposes as partnerships shall apply the credits as provided in subsection (B). If a member is an individual, the limited liability company may earn and pass through any credits allowed by this article to be applied against income tax imposed pursuant to Section 12-6-510. If a member is a corporation, the limited liability company may earn and pass through any credits allowed by this article to be applied against income tax imposed pursuant to Section 12-6-530.

(2) Limited liability companies taxed for South Carolina income tax purposes as corporations are entitled to all credits otherwise applicable to corporations.

(3) With respect to single members of limited liability companies which are not regarded as a separate entity from its owner, members who are individuals may claim any credits allowed by this article to be applied against income tax imposed pursuant to Section 12-6-510 and members which are corporations may claim any credits allowed by this article to be applied against income tax imposed pursuant to Section 12-6-530.

(4) For limited liability companies owned by limited liability companies or other pass through entities described in subsection (B), items (1) through (3) are applied at each successive stage of ownership until the credit is applied against the tax imposed pursuant to either Section 12-6-510 or 12-6-530, as applicable.

Code Section 12-6-3620 provides as follows:

(A) For taxable years beginning after 2007, and ending before taxable year 2020, there is allowed a credit against the income tax imposed pursuant to Section 12-6-530 or license fees imposed pursuant to Section 12-20-50, or both, for twenty-five percent of the costs incurred by a taxpayer for the purchase and installation of equipment used to create heat, power, steam, electricity, or another form of energy for commercial use from a fuel consisting of no less than ninety percent biomass resource. Costs incurred by a taxpayer and qualifying for the credit allowed by this section must be certified by the State Energy Office. The State Energy Office may consult with the Department of Agriculture and the South Carolina Institute for Energy Studies on standards for certifying the costs

incurred by the taxpayer. The credit may be claimed in the year in which the equipment is placed in service and may be claimed for all expenditures incurred for the purchase and installation of the equipment.

(B) A taxpayer may use up to six hundred fifty thousand dollars of credit for a single taxable year. The tax credit is nonrefundable but unused credits may be carried forward for fifteen years.

(C) For purposes of this section:

(1) "Biomass resource" means noncommercial wood, by-products of wood processing, demolition debris containing wood, agricultural waste, animal waste, sewage, landfill gas, and other organic materials, not including fossil fuels.

(2) "Commercial use" means a use intended for the purpose of generating a profit.

(3) If the equipment ceases to use biomass resources as its primary fuel source before the entire credit has been utilized, the taxpayer is ineligible to utilize any remaining credit until it resumes using biomass resources as its primary fuel source (at least ninety percent). The fifteen-year carry forward period must not be extended due to periods of noncompliance.

(D)(1) To obtain the maximum amount of credit available to a taxpayer, a taxpayer must submit a request for credit to the State Energy Office by January thirty-first for all qualifying equipment placed in service in the previous calendar year and the State Energy Office must notify the taxpayer that it qualifies for the credit and the amount of credit allocated to the taxpayer by March first of that year. A taxpayer may claim the maximum amount of the credit for its taxable year which contains the December thirty-first of the previous calendar year. The Department of Revenue may require any documentation that it deems necessary to administer the credit.

...

Questions and Answers

1. May ABC passthrough the biomass credit to Member A and then may Member A pass the credit through to its individual shareholders? May the individual shareholders of Member A use the passed through credit against their individual income tax?

Answer: The biomass credit statute provides in relevant part:

...There is allowed a credit against the income tax imposed pursuant to Section 12-6-530 or license fees imposed pursuant to Section 12-20-50, or both, for twenty-five percent of the costs incurred by a taxpayer for the purchase and installation of equipment used to create heat, power, steam, electricity, or another form of energy for commercial use from a fuel consisting of not less than ninety percent biomass resource. ...

Code Section 12-6-3620 does not address the pass through of credits by flow through entities. However, Code Section 12-6-3310(B) provides general rules relating to the pass through of credits by flow through entities. Under Code Section 12-6-3310(B)(1) "Unless specifically prohibited, an "S" corporation, limited liability company taxed as a partnership, or partnership that qualifies for a credit pursuant to this article may pass the credit earned to each shareholder of

the “S” corporation, member of the limited liability company, or partner of the partnership. Under (B)(2), for an “S” corporation owing corporate level tax, a credit must first be used at the entity level with only the remaining credit passing through to the shareholders of the “S” corporation. This provision allows the pass through of the credit by ABC to Member A. It also allows the passthrough of the biomass credit from Member A on to the individual shareholders of Member A. The statute does not provide any limitation on the number of times that a credit may pass through and allows a credit to pass through entities until it ultimately reaches the final individual or corporate member, shareholder, or partner who can use the credit.

The second part of the question posed by ABC concerns the use of the credit by an individual or corporate taxpayer. On its face, Code Section 12-6-3620 appears to preclude the use of the credit against individual income taxes since individual income taxes are imposed under Code Section 12-6-510 while Code Section 12-6-530, the section imposing corporate income taxes, is referenced in the biomass credit statute. Therefore, if the credit is passed through to a corporate member, partner, or shareholder, it is clear that the corporate member, partner, or shareholder would be able to use the credit against its corporate income tax. However, on the face of the biomass credit statute, if the credit is earned by a passthrough entity, such as ABC or Member A, the credit may be able to be passed through to an individual shareholder, member or partner, but would not be able to be used to offset the individual income tax of that individual.

However, under Code Section 12-6-3310(C) a limited liability company not organized as a legal entity which is a taxpayer expressly specified as qualifying for the credits allowed pursuant to this article nevertheless qualifies for such credits and the limited liability company may earn and passthrough the credits to an individual member who may then apply them against his individual income tax under Section 12-6-510. This statute allows ABC to pass through the biomass credit to an individual member and would allow that member to use the credit against his individual income tax, even though the biomass statute seems to restrict the use of the credit to corporate income tax liability. However, in the above situation, Member A is not an individual, but is instead an “S” corporation. Code Section 12-6-3310(C)(4) specifically states that for limited liability companies owned by limited liability companies or other pass through entities described in subsection (B) [which includes “S” corporations such as Member A], items (1) through (3) [which includes the provision above relating to the use of the credit] are applied at each successive stage of ownership until the credit is applied against the tax imposed pursuant to either Section 12-6-510 or Section 12-6-530, as applicable. This provision allows Member A to pass through the credit to its individual shareholders and further allows those individual shareholders to use the credit against their individual income taxes.

The biomass credit can be passed through by ABC to Member A, and Member A may, in turn, pass the biomass credit through to its individual shareholders, who may use the credit against their individual income tax liability under Code Section 12-6-510.

2: Does the fact ABC intends to sell the energy produced by the biomass facility to a related party in addition to non-related third parties have any effect on the ability of the individual shareholders of Member A to claim the biomass credit?

Answer: No. The statute only requires that the energy created by the equipment be for commercial use. “‘Commercial use’ means a use intended for the purpose of generating a profit.”

Code Section 12-6-3620(C)(2)). Therefore, so long as the energy generated by the equipment that is eligible for the biomass credit is used by ABC and the related party to create heat, power, steam, electricity, or another form of energy for commercial use, the energy may be sold to a related party by ABC without affecting the individual shareholders ability to use the biomass credit passed through by Member A.

3: Is the provision of Code Section 12-6-3620 which limits the use of the biomass credit to \$650,000 in a single taxable year, determined at ABC's level, before the pass through of the credit to Member A and the individual shareholders of A, or is it determined at the individual shareholder's level after all credit earned has passed through to the individual shareholders?

Answer: The \$650,000 cap is applied at ABC's level and therefore, the biomass credit that may be passed through by ABC to all its members for their use is limited to \$650,000 in total each year.

Code Section 12-6-6320 provides that the biomass credit is equal to 25% of the costs incurred by a taxpayer for the purchase and installation of eligible equipment and a taxpayer may use up to \$650,000 of credit for a single taxable year. Under the statute, certain requirements must be met in order to claim the credit. One of the requirements that must be met is that the biomass equipment must be certified as qualifying equipment by the South Carolina Energy Office. The provision of the statute that addresses the certification procedures state: "Costs incurred by a taxpayer and qualifying for the credit must be certified by the State Energy Office." "To obtain the maximum amount of credit available to a taxpayer, a taxpayer must submit a request for credit to the State Energy Office by January thirty-first for all qualifying equipment placed in service in the previous calendar year and the State Energy Office must notify the taxpayer that it qualifies for the credit and the amount of credit allocated to the taxpayer by March first of that year. ..."

Under Code Section 12-6-30(1) the definition of "'Taxpayer' includes an individual, trust, estate, partnership, association, company, corporation, or any other entity subject to the tax imposed by this chapter or required to file a return." [emphasis added] While ABC, a limited liability company taxed as a partnership, is not subject to tax, it is required to file a return so it is considered a taxpayer. When dealing with a flow through entity, both the flow through entity itself and the individual members, shareholders or partners of the entity may be taxpayers. However, for purposes of the biomass credit and applying the \$650,000 cap, the taxpayer referenced is the flow through entity itself and not the individuals ultimately offsetting their individual income tax liabilities with the credit. The biomass statute, Code Section 12-6-3620, is not the statute that allows ABC to pass through the credit and which allows the individuals to use the credit against their individual income taxes. That statute is Code Section 12-6-3310. Under the biomass statute, it is ABC that is the taxpayer that is purchasing the qualifying equipment and incurring the eligible costs and therefore, it would be submitting the paperwork to determine the maximum amount of credit available to pass through. Since it is ABC that is purchasing and placing in service the equipment that is the subject of the biomass credit, it is ABC that is earning the credit under Code Section 12-6-3620 and then passing it through to its members, including Member A. Therefore, ABC is the taxpayer that the biomass statute references for purposes of applying the \$650,000 cap set forth in the biomass statute.

4. May ABC have a special allocation provision in its limited liability company agreement, allocating the biomass credit in a different manner than the member's ownership interest in ABC?

Answer: ABC has elected to be treated as a partnership for tax purposes. Under Code Section 12-6-3310(B)(3), for a flow through entity, the amount of credit allowed a shareholder, partner or member is equal to the percent of the shareholder's stock ownership, partner's interest in the partnership, or member's interest in the limited liability company for the taxable year multiplied by the amount of the credit earned by the entity and available for pass through. Limited liability company and partnership matters are controlled by the applicable limited liability company or partnership agreement. These agreements may provide for different allocations of partnership or limited liability company items. To the extent that ABC's limited liability company agreement provides for different allocations of limited liability company items, the allocation of the credit must be consistent with Treas. Reg. 1-704-1(b)(4)(ii) in order to be effective.

5. For individuals receiving and using a biomass credit, may the credit offset any South Carolina sourced income the individual or married filing jointly couple reports on their South Carolina tax return?

Answer: Yes. The biomass credit may offset any income of the individual or married filing jointly couple reported on their South Carolina income tax return.

CAVEAT: This advisory opinion is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting the advisory opinion may not rely on it. If the taxpayer relies on this advisory opinion, and the Department discovers, upon examination, that the facts and circumstances are different in any material respect from the facts and circumstances given in this advisory opinion, then the advisory opinion will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this advisory opinion, changes in a statute, a regulation, or case law could void the advisory opinion.

SOUTH CAROLINA DEPARTMENT OF REVENUE

s/James F. Etter

James F. Etter, Director

November 4, 2011
Columbia, South Carolina