

## **BILL ANALYSIS**

Senate Research Center  
86R25933 CBH-F

H.B. 2545  
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Finance  
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### **AUTHOR'S / SPONSOR'S STATEMENT OF INTENT**

There are concerns that the increasing demand for water accompanying Texas' recent population growth, coupled with drought conditions, has compelled water planners to consider all potential sources of water in their planning efforts, including sources such as seawater, brackish groundwater, and water produced from oil and natural gas extraction activity. It has been further noted, however, that the high costs applicable to treating those potential sources continue to be an impediment to advancing water desalination in Texas.

H.B. 2545, in an effort to provide a new source of water for beneficial use in Texas, seeks to incentivize water desalination by providing a franchise tax credit to desalination operators who treat source water that has a high total dissolved solids concentration, such as water produced in oil or gas drilling.

H.B. 2545 amends the Tax Code to make an entity that owes a franchise tax and holds a permit to operate a water desalination facility with all necessary state and federal permits that produces fresh water of usable quality eligible for a credit. The exact amount of the credit would be based on the total dissolved solids concentrations in the treated water and contingent on the resulting freshwater being put to beneficial use in Texas.

H.B. 2545 requires a permit holder to submit monthly statements to the Texas Commission on Environmental Quality (TCEQ) and to apply for certain certification from TCEQ to be eligible to claim a credit and sets out related provisions.

H.B. 2545 provides for certain carryforward of any unused credit that exceeds that limitation for not more than five consecutive reports and for the sale or assignment of all or part of a credit to an entity that also could sell or assign part of that credit. An entity to which a credit was transferred could apply all or part of that credit against either a franchise tax or oil and gas severance taxes. A credit earned or purchased by a partnership, limited liability company, S corporation, or other pass-through entity could be allocated to the partners, members, or shareholders of the entity in accordance with the provisions of any agreement to be and without regard to the ownership interest in the desalination facility claiming the credit.

H.B. 2545 limits the applicability of its provisions relating to the tax credit for operation of a desalination facility that begins initial operations on or after January 1, 2021, and that treats water under the jurisdiction of TCEQ or the Railroad Commission of Texas. The bill's provisions relating to such a tax credit expire December 31, 2024. The bill establishes that the expiration of those provisions does not affect certain carry-forward credit or those credits for which a taxable entity is eligible after the expiration of those provisions based on source water treated before the expiration date.

H.B. 2545 amends current law relating to franchise tax, oil production tax, and gas production tax incentives for certain desalination facility operations.

### **RULEMAKING AUTHORITY**

Rulemaking authority is expressly granted to the comptroller of public accounts of the State of Texas in SECTION 2 (Section 171.628, Tax Code) of this bill.

Rulemaking authority is expressly granted to the Texas Commission on Environmental Quality in SECTION 2 (Section 171.628, Tax Code) of this bill.

## **SECTION BY SECTION ANALYSIS**

SECTION 1. Amends Section 171.1011, Tax Code, by adding Subsection (g-9), as follows:

(g-9) Requires a taxable entity that is a permit holder to exclude from its total revenue, to the extent included under Subsection (c)(1)(A) (relating to adding certain amounts for the purposes of computing a certain taxable margin for a taxable entity treated for federal income tax purposes as a corporation), (c)(2)(A) (relating to adding certain amounts for the purposes of computing a certain taxable margin for a taxable entity treated for federal income tax purposes as a partnership), or (c)(3) (relating to utilizing a certain manner determined by rules the comptroller of public accounts of the State of Texas (comptroller) is required to adopt for the purposes of computing a certain taxable margin for a taxable entity treated for federal income tax purposes as neither a partnership nor as a corporation), any amount received by the entity from the sale of minerals or materials extracted from water by the desalination facility during the desalination process. Defines, for purposes of this subsection, "desalination facility" and "permit holder." Provides that this subsection expires December 31, 2024.

SECTION 2. Amends Chapter 171, Tax Code, by adding Subchapter L-1, as follows:

### **SUBCHAPTER L-1. TAX CREDIT FOR OPERATION OF DESALINATION FACILITY**

Sec. 171.621. DEFINITIONS. Defines "commission," for purposes of this subchapter, as the Texas Commission on Environmental Quality (TCEQ). Defines "desalination facility" and "permit holder."

Sec. 171.622. ELIGIBILITY FOR CREDIT. Provides that a permit holder that is a taxable entity and that produces fresh water of usable quality at a desalination facility is eligible for a credit in the amount and under the conditions and limitations provided by this subchapter against the tax imposed under this chapter (Franchise Tax).

Sec. 171.623. AMOUNT OF CREDIT; LIMITATIONS. (a) Provides that the total amount of the credit under this subchapter for the period on which a report is based, except as provided by Subsection (d), is equal to:

(1) 50 cents for each 1,000 gallons of source water treated by the permit holder during the period on which the report is based if the source water has a total dissolved solids concentration of more than 5,000 milligrams per liter and the resulting fresh water is put to beneficial use in this state;

(2) \$1 for each 1,000 gallons of source water treated by the permit holder during the period on which the report is based if at least 50 percent of the source water has a total dissolved solids concentration of more than 30,000 milligrams per liter and the resulting fresh water is put to beneficial use in this state;

(3) \$5 for each 1,000 gallons of source water treated by the permit holder during the period on which the report is based if at least 50 percent of the source water has a total dissolved solids concentration of more than 50,000 milligrams per liter and the resulting fresh water is put to beneficial use in this state; and

(4) \$17 for each 1,000 gallons of source water treated by the permit holder during the period on which the report is based if at least 50 percent of the source water has a total dissolved solids concentration of more than

90,000 milligrams per liter and the resulting fresh water is put to beneficial use in this state.

(b) Authorizes the permit holder to treat source water with differing total dissolved solids concentrations during the period on which the report is based. Entitles the permit holder to prorate the credit by the duration of processing time associated with each concentration during the period.

(c) Authorizes treated water to be counted only once in determining the amount of the credit. Authorizes only one permit holder to claim a credit for the same treated water.

(d) Prohibits the total credit claimed for a report, including the amount of any carryforward under Section 171.624, from exceeding the amount of franchise tax due for the report after all other applicable tax credits.

Sec. 171.624. CARRYFORWARD. (a) Authorizes a permit holder, if the permit holder is eligible for a credit that exceeds the limitation under Section 171.623(d), to carry the unused credit forward for not more than five consecutive reports.

(b) Provides that a carryforward is considered the remaining portion of a credit that cannot be claimed in the current year because of the limitation under Section 171.623(d). Provides that a carryforward is added to the next year's installment of the credit in determining the limitation for that year. Provides that a credit carryforward from a previous report is considered to be used before the current year installment.

Sec. 171.625. APPLICATION. (a) Requires a permit holder to apply for a credit under this subchapter on or with the report for the period for which the credit is claimed.

(b) Requires a permit holder to file with a report on which the credit is claimed a copy of each relevant certificate issued by TCEQ under Section 171.626 and any other information required by the comptroller to sufficiently demonstrate that the permit holder is eligible for the credit and the amount of the credit.

(c) Provides that the burden of establishing eligibility for and the amount of the credit is on the permit holder.

Sec. 171.626. MONTHLY STATEMENT; CERTIFICATION. (a) Requires a permit holder, to be eligible for a credit under this subchapter, to submit to TCEQ monthly statements that include, for the preceding month:

(1) the metered volume in gallons of source water treated by the permit holder;

(2) the total dissolved solids concentration of the source water, distinguished according to the concentrations described by Section 171.623(a);

(3) the duration of processing time associated with each concentration described by Section 171.623(a); and

(4) the total dissolved solids concentration of the resulting fresh water.

(b) Requires the permit holder, to be eligible for the credit under this subchapter, to apply to TCEQ for certification that:

(1) the permit holder has, during the reporting period, treated source water in an amount and with a total dissolved solids concentration that qualify for a credit under Section 171.623; and

(2) the resulting fresh water was put to beneficial use in this state.

(c) Requires the permit holder to include with the certificate application any information TCEQ determines is necessary to certify eligibility for the credit and the amount of the credit, including information sufficient to demonstrate that the permit holder has all state and federal permits necessary to operate the desalination facility and the resulting fresh water was put to beneficial use in this state.

(d) Requires TCEQ, if the permit holder provides sufficient information under this section, to issue a certificate of eligibility to the permit holder.

(e) Requires TCEQ to immediately notify the comptroller in writing if TCEQ:

(1) determines that a permit holder that previously received a certificate under this section was not eligible for the certified credit or is no longer eligible for the certified credit; or

(2) takes any action or discovers any information that affects the eligibility of the permit holder for a credit.

Sec. 171.627. SALE OR ASSIGNMENT OF CREDIT; USE OF SOLD OR ASSIGNED CREDIT. (a) Authorizes a permit holder that earns a credit under this subchapter to sell or assign all or part of the credit, and authorizes any entity to which all or part of the credit is sold or assigned to sell or assign all or part of the credit to another entity. Provides that there is no limit on the total number of transactions for the sale or assignment of all or part of the total credit authorized under this subchapter; however, collectively all transferred and retained credits claimed for a period are subject to the maximum total limitations provided by Subsection (b) and Section 171.623(d).

(b) Authorizes an entity to which a credit or part of a credit was sold or assigned, notwithstanding any other provision of this subchapter, to apply all or part of that credit against the tax imposed by this chapter or against the tax imposed by Chapter 201 (Gas Production Tax) or 202 (Oil Production Tax). Prohibits the total credit claimed against the tax imposed by Chapter 201 or 202 from exceeding the amount of tax due for a report after all other applicable tax credits, but authorizes the entity to carry any unused credit forward until the credit is used.

(c) Requires an entity that sells or assigns a credit under this section and the entity to which the credit is sold or assigned to jointly submit written notice of the sale or assignment to the comptroller on a form promulgated by the comptroller not later than the 30th day after the date of the sale or assignment. Requires the notice to include:

(1) the date of the sale or assignment;

(2) the amount of the credit sold or assigned;

(3) the names and federal tax identification numbers of the entity that sold or assigned the credit or part of the credit and the entity to which the credit or part of the credit was sold or assigned;

(4) the amount of the credit owned by the selling or assigning entity before the sale or assignment, and the amount the selling or assigning entity retained, if any, after the sale or assignment; and

(5) for the entity to which the credit or part of the credit was sold or assigned, each type of tax liability against which the entity intends to

apply all or part of the credit, and the amount or percentage that the entity intends to apply against each type.

(d) Provides that the sale or assignment of a credit in accordance with this section does not extend the period for which a credit is authorized to be carried forward and does not increase the total amount of the credit that is authorized to be claimed.

(e) Authorizes a credit earned or purchased by, or assigned to, a partnership, limited liability company, S corporation, or other pass-through entity, notwithstanding the requirements of this subchapter, to be allocated to the partners, members, or shareholders of that entity and claimed under this subchapter or Chapter 201 or 202 in accordance with the provisions of any agreement among the partners, members, or shareholders and without regard to the ownership interest of the partners, members, or shareholders in the desalination facility operated by the permit holder who earned the credit, provided that the entity that claims the credit is required to be subject to the tax imposed under this chapter or Chapter 201 or 202.

Sec. 171.628. RULES. Requires the comptroller and TCEQ to adopt rules necessary to implement this subchapter.

Sec. 171.629. EXPIRATION. (a) Provides that this subchapter expires December 31, 2024.

(b) Provides that the expiration of this subchapter does not affect the carryforward of a credit under Section 171.624 or those credits for which a taxable entity is eligible after the date this subchapter expires based on source water treated before the date this subchapter expires.

SECTION 3. (a) Provides that, subject to Subsection (b) of this section, this Act applies only to a report originally due on or after the effective date of this Act.

(b) Authorizes a taxable entity to exclude amounts from its total revenue as provided by Section 171.1011(g-9), Tax Code, as added by this Act, only on a report originally due on or after January 1, 2021, and before January 1, 2025.

SECTION 4. Effective date: January 1, 2021.