Tax Credits for Renewables Under the Inflation Reduction Act

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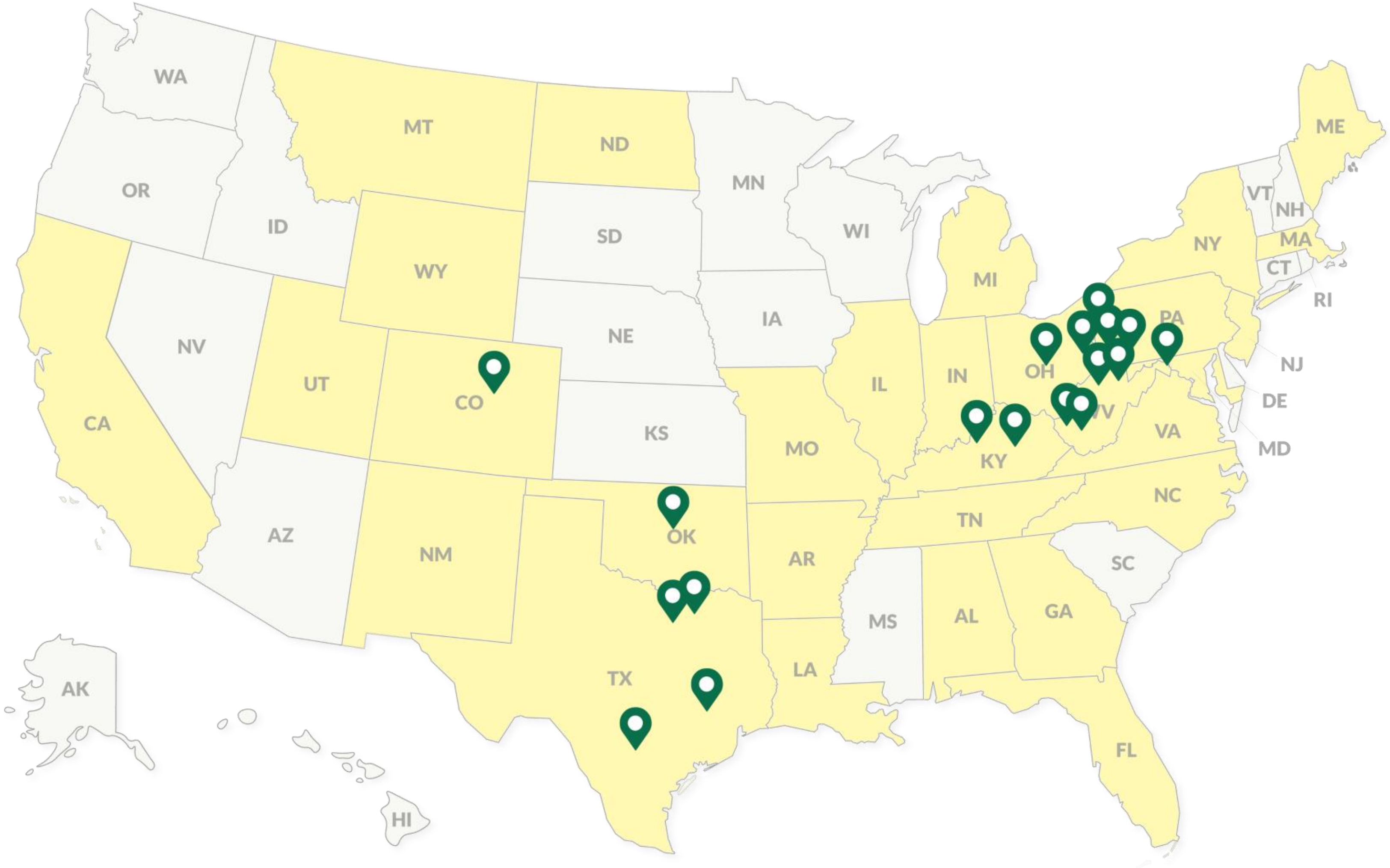

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Inflation Reduction Act

- Federal legislation passed into law in August 2022
- A main focus is on domestic clean and renewable energy production and related technologies
- $370 billion in clean energy investments, according to the White House *Inflation Reduction Act Guidebook* (available at whitehouse.gov/cleanenergy)
- Use of tax credits to provide investments and economic incentives

Tax Credits for Renewables

Investment

IRC Section	Tax Credit
25C	Energy efficient home improvement
25D	Residential clean energy
30C	Alternative fuel vehicle refueling property
48	Energy credit (ITC)
48C	Qualifying advanced energy project
48D	Advanced manufacturing investment (CHIPS Act)
48E	Clean energy investment (ITC replacement)

Production

IRC Section	Tax Credit
40B	Sustainable aviation fuel
45	Renewable electricity production (PTC)
45L	New energy efficient home
45U	Zero-emission nuclear power production
45V	Clean hydrogen production
45Y	Clean electricity production (PTC replacement)
45X	Advanced manufacturing
45Z	Clean fuel production

Tax Credits for Renewables

Deductions

IRC Section	Tax Deductions
168(e)(3)(B)(viii)	Accelerated depreciation for qualified clean energy
179D	Energy efficient commercial buildings

Other

IRC Section	Tax Credit
Vehicles	
25E	Previously-owned clean vehicles
30D	Clean vehicle
45W	Commercial clean vehicle
Other	
45Q	Carbon oxide sequestration

Changes to Investment Tax Credit

	IRC Sec. 48 Energy Credit	IRC Sec. 48E Clean Energy Investment
Placed-in-service date	Before Jan. 1, 2025	After Dec. 31, 2024
Base credit	Lowered to 6% unless certain requirements are met	6% with increases for meeting certain requirements
Qualifying property and technology	Energy storage technologies, microgrid controllers, fuel cells, geothermal (heat pump and direct use), combined heat & power, microturbines, and some interconnection costs	Not technology specific; facilities that generate electricity with a greenhouse gas emissions rate that is not greater than zero and qualified energy storage technologies
Miscellaneous	Expands on solar equipment; recent expansion for biogas property and upgrading equipment	Phase-out once U.S. greenhouse gas emissions are 25% of 2022 emissions

Recapture

- Applies to ITC and 45Q carbon oxide sequestration credit
- ITC –
  - Must repay a percentage of the credit claimed if property is transferred or ceases to be eligible for the credit
  - Five-year period
- 45Q carbon oxide sequestration credit
  - Occurs when carbon oxide for which the credit was claimed ceases to be disposed of in secure geological storage or used as a tertiary injectant
  - Must measure leakage each year versus amount placed in secure storage
  - Three-year period after the last tax year the taxpayer claims the credit

Changes to Production Tax Credit

	IRC Sec. 45 Renewable Electricity Production	IRC Sec. 45Y Clean Electricity Production
Placed-in-service date	Before Jan. 1, 2025	After Dec. 31, 2024
Base credit	Lowered to 0.3 cents/kW (inflation adjusted) unless certain requirements are met	0.3 cents/kW (inflation adjusted) with increases for meeting certain requirements
Qualifying property and technology	Facilities generating electricity from wind, biomass, geothermal, solar, small irrigation, landfill and trash, hydropower, and marine and hydrokinetic renewable energy	Not technology specific; facilities generating electricity for which the greenhouse gas emissions rate is not greater than zero

Election: ITC v. PTC

- IRC Sec. 48(a)(5) – for certain projects, can elect to treat facilities that otherwise qualify for PTC as energy property that qualifies for ITC
- Factors:
  - Higher capacity → PTC
  - Higher capital costs → ITC
  - Bonuses and increases → ITC

Retrofitted Property (80/20 Rule)

- Placed-in-service date and original use
- Fair market value of used property is not more than 20% of facility's total value
- Public commentary:
    - Unfair
    - Discourages use of existing infrastructure
    - Limits investment
    - Significant upgrades to facilities will not qualify

Credit Bonuses and Increases

Prevailing Wage & Apprenticeship	Energy Community
Domestic Content	Low Income Communities

Prevailing Wage & Apprenticeship Requirements

- Credit amount increases 5X
  - Example – 30% versus 6% for ITC
- **Prevailing wage** - All laborers and mechanics are paid not less than prevailing rates (as determined by Department of Labor/Davis-Bacon Act) for construction, alteration, and repair of projects
- **Apprenticeship** – Employ apprentices from registered apprenticeship programs for specific labor hour, apprentice-to-journey worker ratios, and participation requirements
- IRC Sec. 45(b)(7)-(8) and Treas. Regs. Sec. 1.45-7 and -8

Prevailing Wage & Apprenticeship Requirements

IRC Section	Tax Credit
30C	Alternative fuel vehicle refueling property
45	Renewable electricity production (PTC)
45L	New energy efficient home*
45Q	Carbon oxide sequestration
45U	Zero-emission nuclear power production*
45V	Clean hydrogen production
45Y	Clean electricity production (PTC replacement)
45Z	Clean fuel production
48	Energy credit (ITC)
48C	Qualifying advanced energy project
48E	Clean energy investment (ITC replacement)
179D	Energy efficient commercial buildings deduction
**Only prevailing wage requirements apply*	

Domestic Content

- To qualify for the domestic content bonus, a clean energy project must satisfy two requirements:
  - Must use 100% domestic steel and iron for structural construction materials
  - Projects that begin construction before 2025 must use at least 40% domestically manufactured products. This requirement increases 5% annually for projects that begin in 2025, 2026, and 2027, maxing out at 55% in 2027 and after.
- Bonus amounts:
  - For projects that also meet the prevailing wage and apprenticeship requirements, for qualifying projects, the ITC is increased by 10% (percentage points) and the PTC is increased by 10%
  - If a project does not meet prevailing wage and apprenticeship requirements but meets the domestic content minimums, the ITC bonus is decreased

Energy Community

- IRC Sec. 45D provides bonus ITC amounts for clean energy projects located in "energy communities," which are communities historically dependent on fossil energy jobs and tax revenues
- Per Treasury Dept. guidance, energy communities include:
  - A census tract where a coal mine closed after 1999, or where a coal-fired electric generating unit was retired after 2009, qualifies as an energy community, as well as directly adjoining census tracts.
  - A metropolitan statistical area or non-metropolitan statistical area must have or have recently had at least 0.17 percent direct employment, or at least 25 percent local tax revenues related to the extraction, processing, transport, or storage of coal, oil, or natural gas, as well as an unemployment rate at or above the national average unemployment rate for the previous year.
- The bonus is also available for sites typically known as "brownfield" sites: defined as real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant, and includes certain mine-scarred land
- For qualifying projects, the ITC is increased by up to 10% (percentage points) and the PTC is increased by 10%

Low Income Communities

- IRC Sec. 48(e) provides bonus ITC amounts for clean energy projects meeting environmental justice requirements:
  - Projects must be less than $5MW_{AC}$
  - Requires allocation by Treasury - capped at 1.8 GW_{DC} per year
  - Projects can't be placed in service before applying for allocation

Category (Adder Percentage)	Annual Allocation
Category 1: Located in Low-Income Communities (10%)	700 MW
Category 2: Located on Indian Land (10%)	200MW
Category 3: Qualified Low-Income Residential Building Project (20%)	200MW
Category 4: Qualified Low-Income Economic Benefit Project (20%)	700MW

Monetizing the Tax Credits

- IRC Sec. 38 general business credit
- Nonrefundable credit with limitations
- Generally can offset up to 75% of taxpayer's liability
- Consists of several credits including tax credits for renewables, work opportunity, low-income housing, and enhanced oil recovery
- Claim on annual tax return (IRS Form 3800)
- Carryback and carryforward (IRC Sec. 39)
  - Carried back one year and forward 20 years
  - Clean energy credits – carried back three years and forward 22 years

Monetizing the Tax Credits

- Dollar-for-dollar reduction in tax liability
- Refundable vs. nonrefundable tax credits
- Former rules –
  - Tax credits not efficient or useful for nonprofits and tax-exempt entities
  - Had to use tax equity partnerships or sale leaseback structures to enable investors in renewable projects like solar to benefit from the tax credits generated
- IRA changes –
  - Direct/Elective Pay Election – cash payment from the IRS
  - Transferability Election – selling tax credits

Direct/Elective Pay Election

- Tax-exempt organizations, states and local governments and agencies (e.g., school districts, public universities), Indian tribal governments, Alaska Native Corporations, the Tennessee Valley Authority, and rural electric co-operatives
- Not available for for-profit businesses
  - Exception for a few credits – election available for five years
- Receive cash payment from Treasury/IRS by filing annual tax return
- Refundable tax credits

Direct/Elective Pay Election

IRC Section	Tax Credit
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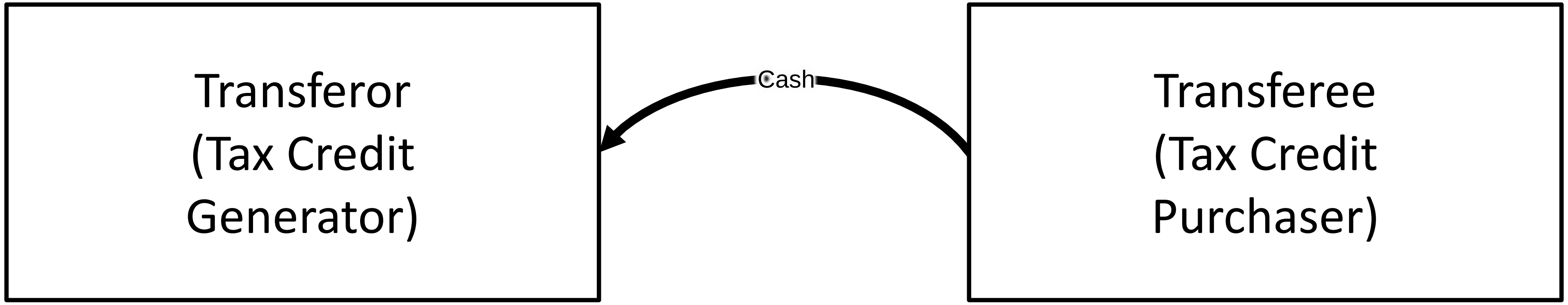
45V	Clean hydrogen production
45W	Commercial clean vehicle
45X	Advanced manufacturing production
45Y	Clean electricity production (PTC replacement)
45Z	Clean fuel production
48	Energy credit (ITC)
48C	Qualifying advanced energy project
48E	Clean energy investment (ITC replacement)

Direct/Elective Pay Election (IRC Sec. 6417)

- Made on original tax return for the tax year the credit is earned
  - Form 990-T (Exempt Organization Business Income Tax Return) if no return is otherwise required
- Made separately for each eligible credit property
- Must register annually with the IRS using pre-filing registration online tool
- Must obtain IRS registration number for each eligible credit property/facility
- Cannot make election for any transferred credit
- *See* Prop. Regs. Sec. 1.6417-1 *et seq.*

Transferability Election



- Sells tax credits to Tax Credit Purchaser in exchange for cash
- Amount received not taxable income
- Can't be a tax-exempt/governmental organization

- Purchases tax credits from Tax Credit Generator in exchange for cash
- Amount paid not deductible
- Can't be related to the Tax Credit Generator
- Bears responsibility for recapture event

Transferability Election

IRC Section	Tax Credit
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Transferability Election (IRC Sec. 6418)

- Made on original tax return for the taxable year for which the credit is determined
- Made annually and separately for each eligible credit property
- Must register annually with the IRS using pre-filing registration online tool
- Must obtain IRS registration number for each eligible credit property/facility
- Must file election statement as described in the proposed regulations with annual tax return (*see* Prop. Regs. Sec. 1.6418-2(b)(5))

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Questions?

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