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Inflation Reduction Act: Renewable Energy Tax Credit and Monetization Overview

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Tax Credits for Energy Production, Investment, Storage, and Manufacturing

Renewable Energy Investment and Production Tax Credits

- **Investment tax credit (ITC)** – Credit based on tax basis of energy property
 - Solar; fuel cells; waste energy recovery; biogas; energy storage; geothermal
- **Production tax credit (PTC)** – Credit based on electricity produced and sold from qualified facility during 10-year period from placement in service
 - Wind; biomass; hydropower
 - Can elect to claim ITC in lieu of PTC for certain qualified facilities

IRA Changes to ITC and PTC

- **Extended full ITC and PTC** for projects construction of which begins before 2025
- **PTC re-expanded** to geothermal and solar
- **ITC expansion** to energy storage technology

Prevailing Wage and Apprenticeship Requirements

- IRA reduced ITC and PTC (and other credits) to 1/5th of prior amount, but added a 5-times multiplier if prevailing wage and apprenticeship requirements met
- Requirements do not apply to projects that are less than 1 MW_{AC} or construction of which began before January 29, 2023
- Preliminary guidance issued, but more expected
- Good faith effort exception to apprenticeship requirement

New Tax Credit “Adders”

- IRA provides increase to ITC and PTC credit amounts for projects that satisfy certain requirements
- **Domestic Content** – All steel and iron and (generally) 40% of manufactured products included in project manufactured or produced in United States
- **Energy Communities** – Projects placed in service in certain areas
- **Low-income Communities** – Projects placed in service in certain areas or that serve low-income communities

Additional Changes

- Extended and modified other business tax credits and individual tax credits
 - Carbon oxide sequestration
 - Zero-emission nuclear power production
 - Biodiesel, renewable diesel, and alternative fuels
 - Clean hydrogen production
 - Alternative refueling property
 - Energy efficient home improvement
 - Residential clean energy credit
- Added “tech-neutral” replacements to ITC and PTC for projects placed in service after 2024
 - Generally work similarly to existing ITC and PTC
 - Does not list specific technologies that qualify
 - IRS will publish guidance identifying types of projects that have greenhouse emissions rate of 0

U.S. Manufacturing

- Many changes to investment and production credits (and direct pay) based on satisfying U.S. sourcing requirements
- **Existing qualifying advanced energy project credit** – Based on tax basis in manufacturing facility in U.S.
 - Requires application for and allocation of credit from IRS
- **New advanced manufacturing production credit** – Based on actual production of certain eligible components produced in U.S.
 - Solar panel components; wind components; battery components
- Must choose one or the other

Tax Credit Monetization

Pre-IRA Paradigm

- **Partnership Flip Structure** – Investors with tax liability investing in renewable energy projects that generate tax credits and other tax benefits (bonus and accelerated depreciation) through a partnership with sponsor
 - Based on complicated partnership tax rules
 - Require significant structuring and cost
- **Lease-Passthrough (ITC)** – Typically in conjunction with partnership flip structure
 - Sponsor entity leases project to (partnership flip) lessee
 - Tax election to treat lessee as owner of project for purposes of ITC
- **Sale-Leaseback (ITC)** – Simpler in many ways than a partnership flip
 - Sponsor sells project to investor and investor leases-back to sponsor
 - Other issues, like prepaid rent and economic substance

IRA Monetization

- **“Direct Pay”**
 - Generally available only to tax-exempt, government, and other specified entities
 - “Normal” taxpayers can make an election for clean hydrogen production, carbon oxide sequestration, and advanced manufacturing production credits
 - Credits generally non-refundable – Election to treat as payment
 - Opens significant new opportunities – Previously many of these entities were kept out of tax benefits associated with renewable energy
 - Must satisfy certain domestic content requirements beginning in 2024 for some credits
- **Tax Credit Transfer**
 - For everyone else that cannot elect Direct Pay
 - Sell tax credits for cash (only)
 - Issues: Election, filing, and pre-filing; ITC recapture; excessive credit transfer (and penalty); passive activity rules; pass-through entity transferors and transferees
- Proposed Regulations issued on June 14, 2023
 - Cannot transfer credit to Direct Pay-eligible person and have them elect Direct Pay
 - Lease-passthrough structure generally not eligible for either election