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Guidance on the Direct Payment of the Inflation Reduction Act's Clean Energy Tax Credits

The Inflation Reduction Act (IRA) inaugurates a substantial shift in American energy policy that will, if implemented thoughtfully, usher in a decades long clean energy infrastructure buildout. Its primary incentive for clean energy generation is the clean energy tax credit program, a continuation and expansion of the tax credit programs passed over a decade ago. Numerous tax credit provisions are of special interest to governments and other public agencies at the federal, state and local levels.

For the first time, the IRA makes tax-exempt public entities eligible for the benefits under these programs through a direct payment provision (referred to herein as direct pay). Prior to this change, tax-exempt entities had been ineligible to receive the investment incentive benefits, in essence locking a large group of potential participants out of the program. With direct pay, public entities that do not have tax liability will be eligible to receive the full value of the incentives as a rebate from the Treasury.

This is important for several key reasons. First, the change unlocks a huge pool of potential clean energy investors that were previously excluded from the program. Governments and public agencies leverage hundreds of billions of dollars each year from the municipal bond market, often to make significant infrastructure investments. These actors will now be able to participate in and accelerate the clean energy infrastructure buildout.

Second, public agencies and governments have unique qualities as market participants that allow them to advance additional social, environmental and political goals in conjunction with energy investment projects. Public investors are more willing and able to make somewhat riskier investments such as advanced nuclear energy. Public actors can also advance local and regional development goals for which market incentives may be insufficient. For example, tribal governments may now build tribe-owned energy infrastructure and use the investments as broader economic development policy that creates good jobs and generates public revenue. Finally, public actors have a strong incentive to develop projects in line with regional energy planning goals, like prioritizing transmission interconnections and connecting those projects to public power pools or municipal aggregation arrangements.

Center for Public Enterprise has submitted the following comments to the IRS regarding implementation of these clean energy programs in the hope that regulators will consider two key guiding principles for direct pay. First, the program should be as expansive as possible: the more participants in the clean energy buildout, the better. Second, the program should create as much simplicity and predictability for public actors as possible in order to incentivize the highest level of participation that is feasible. By taking this approach, the federal government will be handing a powerful tool to public actors across the country to drive the clean energy buildout further, faster, and smarter.

Summary of comments

The Center for Public Enterprise seeks guidance from the IRS that maximizes the opportunity under the statute for America's public agencies to participate in our clean energy transition. In general, we believe that the more participants who are engaged in clean energy investment, development and deployment, the better. The IRS has an opportunity to leverage and bolster the capacity of the public sector by promulgating guidance that incentivizes agency and government participation through simple and broad standards that create certainty for those potential public sector participants.

Below are detailed comments and questions for which the Center for Public Enterprise seeks guidance in service of the above stated goals for the clean energy tax credit programs on topics including agency eligibility, disbursement timelines, project requirements, and other program attributes concerning specific types of projects.

Recommendations and requests for clarification on direct payment of tax credits

1. The IRA's Section §6417(c)(1)(A) defines the term "applicable entity" to mean any organization exempt from tax imposed by subtitle A, any State or political subdivision thereof; the Tennessee Valley Authority; an Indian tribal government (as defined in § 30D(g)(9)); any Alaska Native Corporation (as defined in § 3 of the Alaska Native Claims Settlement Act (43 U.S.C. 1602(m)); or (vi) any corporation operating on a cooperative basis that is engaged in furnishing electric energy to persons in rural areas.

   Future implementation guidance for §6417 and §6418 should expansively interpret "applicable entity" so as to not disqualify entities that clearly fall under the letter and spirit of this definition: public utility districts, rural electric cooperatives, and other quasi-public agencies.[1] The exclusion of any tax exempt entities should be explicitly stated, justified, and made public for comments prior to inclusion in any guidance. Further, potential direct pay recipients would benefit from guidance on the following issues related to entity eligibility:

   a. The IRS should clarify how or if the use of contracting or subcontracting for key project functions by a tax exempt entity affects the eligibility of tax exempt entities for direct pay.

   b. The IRS should clarify whether special purpose public entities established by governments, such as joint action agencies, economic development corporations, joint

[1] This list of possible tax-exempt entities is not intended to be exhaustive.

powers authorities and other such entities are eligible for direct pay. State and local governments often establish and use such special purpose public entities to facilitate investment and development of public works projects for various reasons, including simplifying financing, accounting, contracting and project management. IRS guidance on entity eligibility should strive to create certainty for these potential program participants.

c. The IRS should clarify how or if the involvement of a tax exempt entity in a partnership including entities that are regular taxpayers alters that entity's eligibility for direct pay. For example, would the eligibility of a tax exempt entity involved in such a partnership change if the partnership itself does not claim the right to make a direct pay elections? Clarity here will help create certainty for many smaller public entities or agencies who will likely find such partnerships useful for building the capacity necessary to achieve final deployment of the clean energy resource while avoiding partnership terms that disqualify them from direct pay.

2. The disbursement of direct payments under § 6417 should be quarterly or monthly. Based on when eligible entities indicate their election of direct payment to the IRS, the eligible entities should receive their direct payment benefit as a lump sum payment. Public entities claiming direct pay will require payment-certainty when undertaking project planning and will benefit from a clearly stated and regularized disbursement schedule.

3. The IRS should strive to create simplicity in the filing process for tax exempt entities by limiting paperwork. Any form used to claim a direct payment election should not be overly burdensome so as to ensure efficient filing and processing.

Recommendations and requests for clarification on the tax credits

1. Guidance from the IRS should endeavor to minimize the paperwork and filing requirements in order for public entities to claim the tax credits and receive direct pay benefits and to qualify for the higher value of credits awarded to those meeting domestic content requirements and or qualifying as an energy community. Smaller public entities in particular cannot afford the legal costs associated with overly complex forms.

2. The IRS should provide clarity on when it intends to publish the guidance necessary for projects to determine the cutoffs for eligibility for projects beginning operation this year or whose

construction is soon to begin prior to January 2025. Publishing guidance in a timely manner will provide projects that have not yet started construction but plan to do so within the interim period additional certainty on the full value of the current versions of the Investment or Production Tax Credits they will be able to claim.

3. The IRS should comment on when it anticipates publishing guidance on the revised versions of the Investment or Production Tax Credits that will be available from January 2025 onward. Publishing guidance in a timely manner will provide projects with further certainty on their cash flow and will further encourage them to make their planned investments if they can be sure they will be able to receive the credit.

4. The IRA establishes a Section 45U Production Tax Credit for existing zero-emission nuclear facilities with the intention of mitigating the economic incentive towards their decommission. The specific value of the credit is a function of "gross receipts," however, this definition is ambiguous and potentially introduces biases across nuclear project owners that reflect differences in their contractual arrangements that may undermine the spirit of the provision. We seek clarification on how the IRS intends to treat the definition of gross receipts.

5. The IRA provides clear exceptions to domestic content and apprenticeship requirements based on the acknowledgement that available supply of labor or domestically sourced materials may be prohibitively difficult. The IRS should ensure that the process by which a taxpayer claims these exceptions should be simple and avoid undue paperwork. Examples of potential cases where this could be particularly useful to municipalities or smaller public agencies claiming these cases are listed below. Furthermore, public agencies and other tax exempt entities that are located in energy communities will be more vulnerable to the high costs and project delays if meeting the labor or domestic content requirements becomes too prohibitive due to forces outside their control.

    a. Tax credit recipients may qualify for an exception to domestic content requirements if the inclusion of "steel, iron, or manufactured products which are produced in the United States increases the overall costs of construction of qualified facilities by more than 25 percent" or the "relevant steel, iron, or manufactured products are not produced in the United States in sufficient and reasonable quantities or of a satisfactory quality." The IRS should ensure that the guidance on what qualifies as "steel, iron, or manufactured products," "sufficient and reasonable quantities," or "satisfactory quality" are not unduly

prohibitive of real cases faced by either energy communities or tax exempt filers (HR 5376, §13101 (g) (10) (D)).

b. The IRA allows a taxpayer to claim an exemption from apprenticeship requirements if the denial of its request for qualified apprentices from a registered apprenticeship program was not the result of a refusal of contractors or subcontractors to comply with requirements of the registered apprenticeship program or if the registered program fails to respond to the request within five business days. The IRS should clarify whether tax exempt entities receiving this credit are also eligible to use this exception. The IRS should further clarify whether the exception applies if the denial was due to the lack of available labor in the region. This in particular is a condition that labor pools in or near energy communities may be particularly susceptible to (HR 5376, §13101 (f) (8) (D)).