INFLATION REDUCTION ACT: IMPLICATIONS FOR RENEWABLES AND ENERGY TRANSITION

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IRA Overview – Two-Tier Tax Credit Structure

- Projects that qualify for tax credits automatically get a "**base rate**."
- Projects can get an "**increased rate**" worth 5x the base rate if **prevailing wage** and **apprenticeship** requirements are met. Certain projects are exempt.
  - Prevailing wage = Wages at prevailing rates for similar work at the project local as determined by the Department of Labor.
    - Applies to laborers and mechanics during applicable tax credit period.
  - Apprenticeship = Minimum percentage of total labor hours to construct facility are performed by "qualified apprentices" who participate in a registered apprenticeship program that complies with certain federal requirements.
    - Percentage is 10% for 2022, 12.5% for 2023, and 15% after 2023.
- Exempt projects:
  - Began construction before passage of Treasury guidance on apprenticeship/prevailing wage + 60 days.
  - Less than 1 MW (AC) projects.

IRA Overview – Adders

- Domestic Content
  - Up to 10% adder for PTC or ITC.
  - Requires project to incorporate a sufficient amount of products produced in US (generally beginning at 40% and scaling up to 55%).
- Energy Community
  - Up to 10% adder for PTC or ITC.
  - Energy Communities:
    - Brownfield Sites.
    - Areas with employment or tax revenues relating to coal, oil, or natural gas and above average unemployment.
    - Areas in which a coal mine or a coal-fired electric generating plant has closed.
- Low-Income Community
  - Up to 20% adder to the ITC for solar and wind projects located in certain low-income communities, low-income residential building projects, or on Indian land.
  - Dependent on receiving "environmental justice" capacity allocation from Treasury.

IRA Overview – Direct Pay and Transferability

- Direct Pay
  - Allows taxpayers to receive value of the PTC or ITC from a cash refund payment from the IRS.
  - Avoids need to have sufficient tax liability to take advantage of the credit.
  - Mostly limited to certain tax-exempt entities (including municipalities and state and local governments).
  - Taxable entities can elect direct pay for a limited subset of credits: carbon sequestration, hydrogen production, and advanced manufacturing.
  - Same concept was in the BBBA, but this is more limited.
- Transferability
  - Allows taxpayer to sell PTC or ITC outright to an unrelated person for cash.
  - As with direct pay, avoids need to have sufficient tax liability to take advantage of the credit.
  - New concept.

IRA Overview – PTCs

- Unreduced base/increased PTC rates apply to projects that place in service in 2022 or later.
  - Projects that are already in service are stuck with existing phasedown schedule.
- PTC projects are eligible for adders beginning in 2023.
- Solar is newly eligible for PTCs.
- Section 45 PTC replaced by 45Y PTC in 2025.
  - Electricity must be sold to an unrelated party unless the facility is equipped with a metering device owned and operated by an unrelated person.
  - Facility must have a zero greenhouse gas emissions rate.
- New 45Y PTC starts phasing down for projects that start construction two years after the later of (i) the calendar year in which the Secretary of the Treasury Department determines that annual greenhouse gas emissions from the production of electricity in the US are 25% or less than 2022 levels, or (ii) 2032.

IRA Overview – ITCs

- Unreduced base/increased ITC rates apply to projects that place in service in 2022 or later.
  - Projects that are already in service are stuck with existing phase down schedule.
- ITC projects are eligible for adders beginning in 2023.
- New ITC for standalone storage facilities (regardless of whether charging is from solar or wind).
- Section 48 ITC replaced by 48E ITC in 2025.
  - Facility must have a zero greenhouse gas emissions rate.
- New 48D ITC starts phasing down for projects that start construction two years after the later of (i) the calendar year in which the Secretary of the Treasury Department determines that annual greenhouse gas emissions from the production of electricity in the US are 25% or less than 2022 levels, or (ii) 2032.

IRA Overview – Carbon Capture and Sequestration

- Under current law, beginning in 2025, the credit is $50 a metric ton for carbon that is sequestrated and $35 a metric ton for carbon oxide which is used either in enhanced oil recovery or which is utilized in certain processes.
  - The credit extends for 12 years after the carbon capture equipment is placed in service.
  - To be eligible for the credit, construction of the facility must begin prior to 2026.
- The IRA would both extend the existing credit for projects that begin construction before 2033, and increase the credit value as illustrated in the table on the next slide.
- Consistent with PTCs and ITCs, the 45Q credit would take on a two-tier approach.
- The credit amounts would be significantly increased, especially for carbon oxide captured through direct air capture.

IRA Overview – Carbon Capture and Sequestration (cont'd)

The revised credit amounts would be as follows:

End Use	Current Law	Base	Increased Credit
<u>Traditional Carbon Capture</u> Carbon Oxide Used or Utilized	$35	$12	$60
Carbon Oxide Sequestrated	$50	$17	$85
<u>Direct Air Capture</u> Carbon Oxide Used or Utilized	$35	$26	$130
Carbon Oxide Sequestrated	$50	$36	$180

- The IRA would significantly reduce the minimum capture amounts required to qualify for the credit, some as low as 1,000 metric tons annually for direct air capture, with most requiring 12,500 metric tons annually.
- The revised 45Q provisions are effective for facilities or equipment placed in service after 2022.

IRA Overview – Hydrogen

- The IRA also includes long-awaited and significant incentives for the production of clean hydrogen under a new section 45V.
- The provisions are designed to enable both blue hydrogen and green hydrogen to qualify for the credit.
- Similar to PTCs for other technologies, the tax credit will be available for 10 years beginning on the date the facility is placed in service. The credit amounts would vary depending on the level of greenhouse gas that is removed and is subject to the same two-tier “base rate” and “increased rate” of other renewable energy credits. The maximum increased rate is $3.00 a kg.

IRA Overview – Hydrogen (cont'd)

The credit amount is multiplied by five if prevailing labor and wage standard requirements are met.

CO2 Per KG of H2 Remaining After Removal	PTC Credit Percentage	PTC Value
Not greater than 4 kg and less than 2.5 kg	20%	$.60
Less than 2.5 kg and not less than 1.5kg	25%	$.75
Less than 1.5 kg and not less than .45kg	33.4%	$1.00
Less than .45kg	100%	$3.00

- As an alternative, the taxpayer may elect to take an ITC equal to a percentage of the cost of the facility. The credit amounts would vary depending on the level of greenhouse gas that is removed and is subject to the same two-tier "base rate" and "increased rate" regime as the PTC.

IRA Overview – Hydrogen (cont'd)

The base rate for the ITC is 6%, subject to similar limitations as illustrated below.

CO2 Per KG of H2 Remaining After Removal	PTC Credit Percentage	ITC Value
Not greater than 4 kg and less than 2.5 kg	20%	1.2%
Less than 2.5 kg and not less than 1.5kg	25%	1.5%
Less than 1.5 kg and not less than .45kg	33.4%	2%
Less than .45kg	100%	6%

- The IRA would facilitate the pairing of clean hydrogen facilities with wind and solar farms for which PTCs may be claimed apart from the clean hydrogen tax credits. It would do so by relaxing a PTC rule barring sales between related parties, opening the door to common ownership of both the hydrogen facility and any renewables project that powers it.

IRA Overview – Hydrogen (cont'd)

- The hydrogen production credit would not be available for hydrogen produced at a facility which includes carbon capture equipment for which the credit under section 45Q is claimed, even if in a prior taxable year.
- The provisions are applicable for hydrogen produced after 2022 or, for purposes of the ITC, to facilities placed in service after 2022.

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