Initial IRS Guidance on Two Energy Investment Tax Bonus Credits

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On February 13, 2023, the U.S. Treasury Department, together with the U.S. Department of Energy (DOE) and the Internal Revenue Service (IRS), released its initial guidance on two key provisions of the Inflation Reduction Act of 2022 (IRA) designed to incentivize investment in (1) qualifying advanced energy projects (Section 48C Program[1]) and (2) solar and wind energy projects in low-income communities (Section 48(e) Program).

These two separate programs, representing billions of dollars in potential tax savings for the energy industry, are designed to attract new investments in renewable energy projects and new job opportunities in targeted communities. Developers and real estate owners in coal communities should carefully review the qualifying requirements and timeline below. Frost Brown Todd LLP has significant experience advising clients who have invested in development projects in targeted communities.

Advanced Energy Project Credit Allocation Program

IRS Notice 2023-18 establishes the program by which the Treasury Department will allocate a cumulative $10 billion of credits (at least $4 billion of which must be allocated to projects located in Energy Communities Census Tracts (i.e., coal communities)) for qualified investments in eligible advanced energy projects. In order to claim this credit, a taxpayer must apply for and receive certification from the Treasury Department that a project qualifies as an advanced energy project. The timeline for the Advanced Energy Project Credit Allocation Program is set forth below.

Amount of Credit

The Section 48C credit, originally enacted by Section 1302(b) of the American Recovery and Reinvestment Act of 2009, has been recently amended by the IRA to extend its timeline and provide an

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additional credit allocation of $10 billion.

The amount of the Section 48C credit for any taxable year is equal to a certain percentage of the qualified investment for any qualifying advanced energy project of the taxpayer. Section 48C(e)(4)(A) provides for an initial base credit rate of 6% of the qualified investment. However, Section 48C(e)(4)(B) increases this amount to an alternative rate of 30% of the qualified investment if prevailing wage and apprenticeship requirements are met. Generally, the credit is allowed in the taxable year in which the eligible property is placed in service.

Qualifying Advanced Energy Project

A qualifying advanced energy project includes a project that re-equips, expands or establishes an industrial or manufacturing facility for the production or recycling of the following:

- Property designed to be used to produce energy from the sun, water, wind, geothermal deposits, or other renewable resources;[2]
- Fuel cells, microturbines, or energy storage systems and components;[3]
- Electric grid modernization equipment or components;[4]
- Property designed to capture, transport, remove, use, or sequester carbon oxide emissions;[5]
- Equipment designed to refine, electrolyze, or blend any fuel, chemical, or product which is renewable, or low-carbon and low-emission;
- Property designed to produce energy conservation technologies (including residential, commercial, and industrial applications);
- Light-, medium-, or heavy-duty electric or fuel cell vehicles, as well as technologies, components, or materials for such vehicles, and associated charging or refueling infrastructure;
- Hybrid vehicles with a gross vehicle weight rating of not less than 14,000 pounds, as well as technologies, components, or materials for such vehicles; and

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- Other advanced energy property designed to reduce greenhouse gas emissions.

Energy Communities Census Tracts

At least $4 billion of the Section 48C credits must be allocated to projects located in Energy Communities Census Tracts (specific census or adjacent tracts that meet the criteria as determined by the DOE) at the time that DOE provides recommendations. Requirements of an Energy Communities Census Tract include:

- Prior to August 16, 2022, the census tract had no project that received a certification and allocation of credits under the Section 48C(d) allocation program established under the 2009 Act; and
- The census tract meets one of the following criteria:

  (a) a census tract in which a coal mine has closed after December 31, 1999;

  (b) a census tract in which a coal-fired electric generating unit has been retired after December 31, 2009; or

  (c) a census tract directly adjoining a census tract that meets of the two preceding criteria.

Allocation Rounds

The first allocation round of the Section 48C Program will begin on May 31, 2023, with an anticipated allocation of $4 billion of qualifying advanced energy project credits (approximately $1.6 billion of which will be allocated to projects located in Energy Communities Census Tracts). To be considered for an allocation of credits for Round 1, taxpayers must submit concept papers to the DOE by July 31, 2023. Following submission of a concept paper, DOE will review and recommend taxpayers to submit a joint application for DOE recommendation and IRS Section 48C certification if it determines that the project has a reasonable expectation of commercial viability. The IRS will consider a project under the Section 48C

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program only if DOE provides a recommendation and ranking for the project.

Timeline

- A taxpayer submits a concept paper to DOE through its online application portal, eXCHANGE, accessible here.
- DOE reviews the concept paper and sends the taxpayer a letter encouraging or discouraging the submission of an application. All taxpayers who submit concept papers are eligible to submit an application, regardless of DOE's response to their concept papers.
- Taxpayers submit applications through the eXCHANGE portal.
- DOE reviews the applications for compliance with eligibility and other threshold requirements. If the application complies with all eligibility and threshold requirements, DOE conducts a technical review of the application to form a DOE recommendation.
- DOE provides a recommendation to the IRS regarding the acceptance or rejection of each Section 48C application and a ranking of the applications.
- The IRS makes a decision regarding the acceptance or rejection of each Section 48C application based on DOE's recommendation and ranking and notifies each taxpayer that submitted a Section 48C application of the outcome by sending an allocation or denial letter.
    - In the case of an acceptance, the amount of Section 48C credits allocated to a project will also be based on the taxpayer's qualified investment in the qualifying advanced energy project and whether the taxpayer intends to apply for and receive an allocation of Section 48C credits calculated at the 30 percent credit rate.
    - In the case of a denial, the taxpayer may be eligible to request a debriefing.
- Within two years of receiving an allocation letter, the taxpayer must notify DOE that the certification requirements have

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been met by submitting this information through the eXCHANGE portal.

- DOE then notifies the taxpayer and the IRS that it has received the taxpayer's notification that the certification requirements have been met.
- The IRS certifies the project by a certification letter.
- Within two years of receiving the certification letter, the taxpayer notifies DOE that the project has been placed in service by submitting such information through the eXCHANGE portal.
    - A taxpayer that does not notify DOE that it has placed the project in service within the required two-year period will forfeit Section 48C credits allocated to the taxpayer for such project.

- DOE notifies the taxpayer and the IRS that it has received the taxpayer's notification that the project has been placed in service or notification that the taxpayer will not place the project in service within the required two-year period.
- If the taxpayer has placed the project in service within the required two-year period and has notified DOE, the taxpayer claims the Section 48C credit on its income tax return for the taxable year in which the project was placed in service.

Additional Section 48C Program guidance will provide further details on the information required to be submitted to DOE in an application for DOE recommendation, along with details regarding the process for applying for DOE recommendation and the instructions for filing concept papers and applications for DOE recommendation. After Round 1, the IRS will conduct additional allocation rounds for the Section 48C Program.

Low-Income Communities Bonus Credit Program

IRS Notice 2023-17 establishes the Low-Income Communities Bonus Credit Program under Section 48(e), setting forth the application process by which the Treasury Department will allocate amounts of "capacity limitation" for a "qualified solar and wind

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facility" that is placed in service to certain low-income communities. The annual capacity limitation is 1.8 gigawatts of direct current capacity for 2023 and 2024, and zero thereafter. For qualifying projects that receive an allocation of capacity limitation from the Treasury Department, the investment tax credit (ITC) percentage will increase by either 10 or 20 percentage points, depending on the category of the facility. Put another way, if the ITC percentage is 30% (i.e., assuming the prevailing wage and apprenticeship requirements are satisfied by the project), the ITC percentage under the Low-Income Communities Bonus Credit Program would increase to either 40% or 50%, as explained more fully below.

A "qualified solar and wind facility" means any facility that (i) generates electricity solely from a wind facility, solar energy property, or small wind energy property; (ii) has a maximum net output of less than 5 megawatts (as measured in alternating current); and (iii) is described in at least one of the following four categories:

Facility Categories		**Capacity Limitation Allocation**	**Bonus Percentage**
Category 1	Low-Income Community	700 megawatts	10%
Category 2	Indian Land	200 megawatts	10%
Category 3	Qualified Low-Income Residential Building Project	200 megawatts	20%
Category 4	Qualified Low-Income Economic Benefit Project	700 megawatts	20%

The 20% bonus percentage applies to eligible property that is part of a Category 3 facility or a Category 4 facility.[6] To be eligible for either the 10% or 20% bonus percentage, the eligible property must be placed in service within four years after the date the applicant

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was notified of the allocation of capacity limitation to the facility where the property is located in.[7]

Details of the application process are expected in additional guidance from the IRS and the Treasury Department; however, Notice 2023-17 states that applications will be accepted in a phased approach for calendar year 2023, during 60-day application windows. The IRS and Treasury Department anticipate applications will be accepted for Category 3 and 4 facilities in the third calendar quarter of 2023 and that applications will be accepted for Category 1 and 2 facilities, thereafter.

The DOE will review the applications for statutory eligibility and will provide recommendations to the IRS regarding the selection of applications for an allocation of capacity limitation. DOE will also perform a lottery or other process for allocation if selected applications exceed the capacity limitations. The IRS will then accept or reject an applicant's request for an allocation of capacity limitation and notify the applicant of its decision with the amount of capacity limitation allocated. Applicants have four years from the date of the acceptance notification to place the property in service.

Transferability of Credits

It is important to note that IRA, under Section 6418, allows certain credits, including the Section 48(e) and Section 48C(e) credit, to be transferred to an unrelated transferee taxpayer. The transfer can relate to all, or a portion specified of an eligible credit, must be paid in cash, and be a one-time transfer (i.e., the transferee may not transfer any portion of its transferred credit). The transfer is not included as income for the recipient taxpayer and is not deductible by the paying taxpayer. The IRA does not allow applicable entities (as defined in the IRA) to elect to transfer credits. The IRS is yet to issue guidance on how credits will be transferred to an unrelated third-party.

Given the magnitude of tax allocation credits up for grabs, energy companies and investors should be on the lookout for additional guidance from the IRS and DOE to ensure their applications are as competitive as possible. For more information about tax-saving

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opportunities, contact Raghav Agnihotri, Brian Masterson, Chris Coffman or any attorneys with Frost Brown Todd's Tax Practice.

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[1] All references to "Section" are to sections of the Internal Revenue Code of 1986, as amended.

[2] Examples include solar panels and specialized support structures; wind turbines, towers, floating offshore platforms, and related equipment.

[3] Examples include stationary batteries; stationary hydrogen fuel cells and storage vessels; microturbines for combined heat and power systems, among others.

[4] Examples include grid equipment for electricity delivery; power flow, control, and conversion, such as transformers, power electronics, among others.

[5] Examples include carbon capture equipment necessary to perform physical action to capture carbon oxide and equipment designed to refine, electrolyze, or blend any fuel, chemical, or renewable product, or low-carbon and low-emission.

[6] The guidance also provides for additional information concerning the four categories for qualified solar and wind facilities, facilities that are described in multiple categories, and the § 48(e) increase that are covered in this article.

[7] The guidance also mentions that the § 48(e) Program will incorporate additional criteria in determining how to allocate the Capacity Limitation reserved for each facility category among eligible applicants, including a focus on facilities that are (i) owned or developed by community-based organizations and mission-driven entities, (ii) encourage new market participants, (iii) provide substantial benefits to low-income communities and individuals marginalized from economic opportunities, and (iv) have a higher degree of commercial readiness. Additional guidance will fully describe these additional criteria.

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