Inflation Reduction Act: Water Related Tax Credit Summary

The Inflation Reduction Act (IRA) provides revisions to existing tax credits and creates new tax credits for green energy projects. The IRA allows non-tax-paying entities such as local governments, to now claim a tax credit without incurring any tax liability. While existing credits are enhanced in the short term, many are also phased out and replaced by zero-emission credits in the future (i.e., timing can be critical).

Tax Credit Types and Eligibility

Energy properties are eligible for one of the following:

- Production tax credits (PTC) – most applicable when energy is sold from a qualified[1] resource
- Investment tax credits (ITC) – most applicable when energy is reused on a qualified property

ENERGY INVESTMENT CREDIT (§48)

With the IRA, ITCs under §48 are increased; however, the IRA also included sunset provisions including for solar and biogas. Construction of solar facilities must begin before January 1, 2025, at which time this credit is replaced by §48E.

Under §48 biogas facilities are more complicated than solar facilities. The facility must meet the definition of a qualified biogas property (see inset) and there is a relatively narrow window of eligibility for biogas projects. Biogas facilities must be placed into service after December 31, 2022; however, construction must begin before January 1, 2025.

[1]Qualified varies by type of credit. See individual credits for more information.

Qualified biogas property means property comprising a system which:

1. converts biomass [defined in 45K(c)(3)] into a gas which is not less than 52% methane (or concentrated to 52%) **and**
2. captures such gas for sale or productive use, and not for disposal via combustion.

QUALIFYING ADVANCED PROJECT ENERGY CREDIT (§48C)

§48C provides an ITC of 30% for qualifying advanced energy project which may include energy reduction (i.e., >20%) projects at treatment facilities. The process to obtain this credit is different than other credits in that a certification must be obtained from US Treasury and there is a limited allocation. Once a certification is obtained, the facility must be placed into service within 3 years. The IRS has defined treatment facilities as "industrial" making them eligible for this credit.

CLEAN ELECTRICITY INVESTMENT CREDIT (§48E)

§48E provides an ITC for technology-neutral (e.g., solar) facilities placed in service after December 31, 2024 (aligns with expiration of credits under §48). Technology-neutral facilities generate electricity with a greenhouse gas emissions rate that is not greater than zero and qualified energy storage technologies. Phase-out of §48E starts the later of 2032 or when certain greenhouse gas emission reductions are met.

CLEAN VEHICLES (§45W AND §30C)

§45W provides a credit for hybrid and electric vehicles placed in service after January 1, 2023 and acquired before January 1, 2033. The amount of the credit is the lesser of (a) 15% of the vehicle's basis (i.e. its cost to the purchaser) or 30% for vehicles without internal combustion engines, or (b) the amount the purchase price exceeds the price of a comparable internal combustion vehicle. The credit is capped at $7,500 for vehicles < 14,000 lbs and $40,000 for all other clean vehicles.

§30C provides a credit associated with the cost of any qualified alternative fuel vehicle refueling property. However, the alternative fuel vehicle refueling property must be placed in service in an eligible census tract. According to the Building a Clean Economy: A Guidebook to the Inflation Reduction Act's Investments in Clean Energy and Climate Action (The White House, Dec 2022), this credit is now available to local governments. The qualifying property must be placed in service before December 31, 2032.

Tax Credit Calculation

The amount of credit depends in many cases on meeting prevailing wage and apprenticeship (PWA) requirements, domestic sourcing, location, etc. For example, Figure 1 shows three scenarios – the base credit, base credit plus credits for domestic procurement and locating in an energy community, and lastly how those credits can be multiplied by meeting PWA requirements. In some cases for small facilities (i.e., <1 megawatt), these additional provisions to obtain a full credit are waived, which may be a sizing consideration. Credits are reduced for tax-exempt financing (there is uncertainty with respect to State Revolving Fund financing). However, the reduction for tax-exempt financing has been trimmed by the IRA.

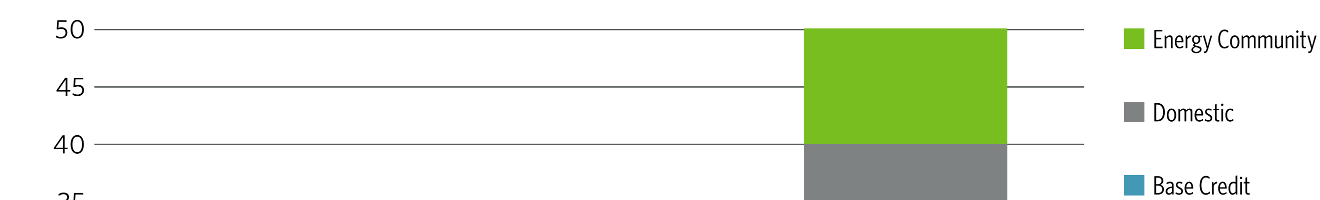

Figure 1 – How meeting prevailing wage and apprenticeship (PWA) multiplies the base, domestic content, and energy community credits

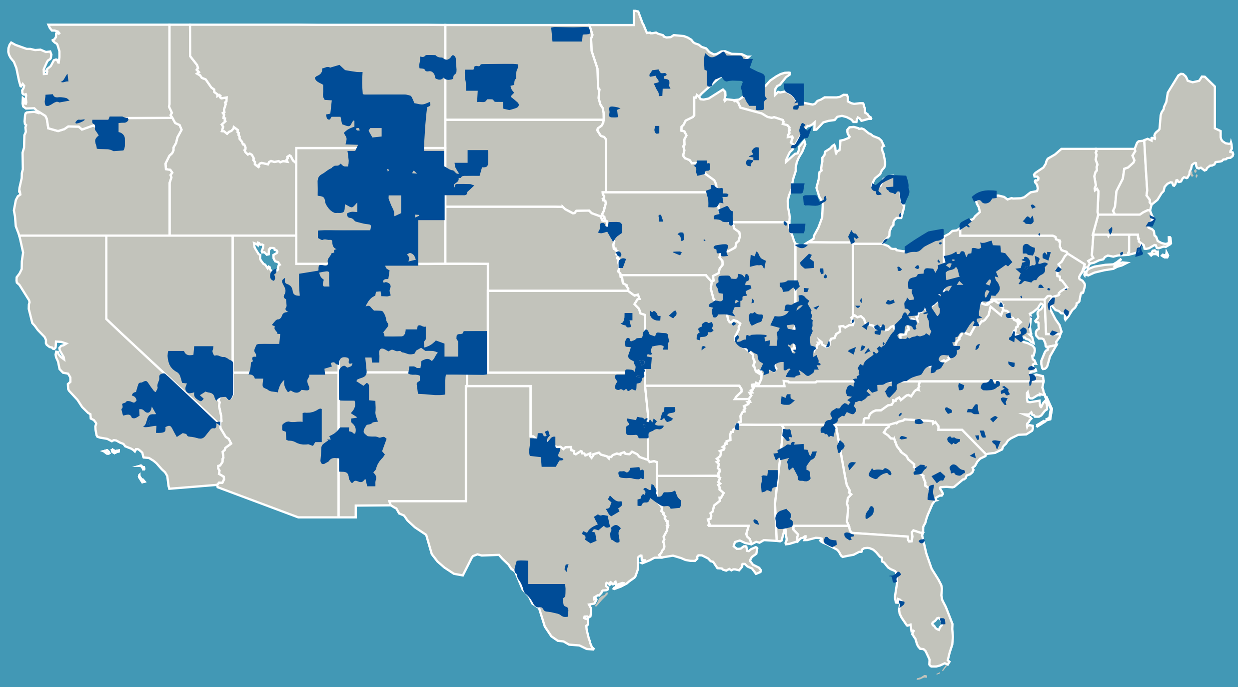

Figure 2 – Energy Communities Map, Source: [Home – Energy Communities]

ENERGY COMMUNITIES

An energy community includes areas in which a coal mine or coal-fired power plant has closed or that have been economically reliant on the extraction, processing, transport, or storage of coal, oil, or natural gas but now face higher-than-average unemployment (see Figure 2). It also includes adjacent census tracts.

The U.S. Department of the Treasury issues guidance on the implementation of the IRA. We recommend attorneys versed in the tax code be consulted early in exploring any credit to fully understand the code, issued guidance, and issues where guidance has not yet been published. The following links provide additional details on these tax credits.

For additional information:

Inflation Reduction Act of 2022 | Internal Revenue Service (irs.gov)

Inflation Reduction Act Guidebook | Clean Energy | The White House

Questions? Please contact:

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