Inflation Reduction Act:

Impacts on Renewable Energy Credits for Exempt Organizations

Overview

- Where We Were Prior to August 2022
- How Tax-Exempt Organizations Participated in Clean Energy Projects Prior to August 2022
- What Does the Inflation Reduction Act (IRA) do for Clean Energy Sector?
- What Does the IRA do for Tax-Exempt Organizations.
  - And What it Doesn't do.
- What Hasn't Changed.
- What's Next ….

Clean Energy Market Pre-August 2022

- Declining Investment Tax Credit Program – 30% had gone to 26%, heading to 22%
  - Gymnastics and expenditures to hit "commence construction milestones."
- Limited technologies available for the credit
- Restrictions on the Production Tax Credit programs
- Practical limitations on Tax-Exempt Organizations participating in the Sector
- In a nutshell, it was business as usual ….

Tax-Exempt Organizations Participation in Clean Energy Before IRA and Direct Pay

- Power Purchase Agreement (PPA) Model.
  - Through a third-party ownership model, clean energy (let's use solar) providers typically own, operate, and maintain the system.
  - Especially valuable because tax credits (along with accelerated depreciation benefits) can be converted into a lower electricity rate, allowing them to go solar with no capital required.
  - Depending on the terms of the PPA, you may choose to purchase the system before the term ends.
  - In this scenario, you are only responsible for purchasing the energy produced by the system based on a customized long-term payment plan at a discount to current market rates.
- Service Agreements
  - A cross between a PPA and Lease, you pay a fixed, monthly amount to use the system for your facility, with adjusters depending on system performance.
  - Depending on the terms of the service agreement, you may choose to purchase the system before the term ends.
  - Operations and maintenance costs are typically covered, and you don't pay for the energy produced.

IRA - Key Takeaways

- Inflation Reduction Act ("IRA") is largely green energy legislation.
- **Increased tax incentives:** By increasing the percentage of the credit from 26% to 30%-40% and expanding the range of possible costs and projects that qualify for benefits, approximately **50%-55% of the cost** of building renewable energy production (solar, wind and other) and storage can be funded with refundable, transferrable tax credits and benefits.
- **More paths to monetization of tax benefits**: The changes open tax benefits to non-taxable entities and individuals who previously did not benefit from them because they either did not have taxable income or they were subject to "passive activity loss" restrictions.
- Because of (1) increased tax credits, (2) more ways to monetize those credits – direct refunds or sale of credits to others and (3) expansion of benefits to new investors like tax exempt organizations and individuals, the **break-even and pay-back has gone from 15 to 20 years to 7 to 8 years**.
- Provides opportunities for exempt organizations to utilize these tax credits where, previously, these organizations would not have benefited.

Inflation Reduction Act: Clean Energy Investment Tax Credits

Until Dec 31, 2024	Highlights	Deadlines to Consider	Additional Details
Extension of Energy Investment Tax Credit (Section 48)	Extends the existing energy investment tax credit for applicable energy projects. This tech-specific ITC ends in 2024 for most technologies and is replaced by the new tech-neutral Clean Electricity ITC (48D), which begins in 2025.	Extends date of construction in most cases to 2024 and maintains a 10% or 30% credit.	• Maintains **30% credit** for solar energy property, geothermal property, fiber-optic solar property, fuel cell property, microturbine property, small wind property, offshore wind property, combined heat and power property, and waste energy recovery property constructed before **January 1, 2025.** • Creates **30% credit** for energy storage technology biogas property, microgrid controllers, dynamic glass, and linear generators constructed **before January 1, 2025.** • **This credit can be up to 40%** if in Opportunity Zones and designated rural areas. *More later in this presentation* • Extends **10% credit** for microturbine projects constructed before **January 1, 2025.** • **30% credit** for geothermal heat pump projects constructed before **January 1, 2033**. • Credit reduces to **26% in 2033** and **22% in 2034**.

Inflation Reduction Act:
Clean Energy Investment Tax Credits

New in 2025	Highlights	Deadlines to Consider	Additional Details
New Clean Electricity Investment Tax Credit (48D)	This newly established, tech-neutral ITC (48D) replaces the above Energy ITC once it phases out at the end of 2024. 48D is an emissions-based incentive that is neutral and flexible between clean electricity technologies**.** **Taxpayers choose between a PTC (45Y) and an ITC (48D).**	Credits are set to phase out the later of **2032 or when emission targets are achieved** *(i.e., the electric power sector emits 75% less carbon than 2022 levels).*	• Creates an ITC credit of 30% of the investment in the year the facility is placed in service. • Clean electricity projects smaller than 5 MW can include the costs of interconnection under the ITC. • The Treasury Department is directed to publish emission rates for similar technologies each year for taxpayers to use for purposes of determining their eligibility. • Facilities will be able to claim a credit at 100% value in the first year, then 75%, then 50%, and then 0%.

Inflation Reduction Act: Clean Energy Investment Tax Credits

	Highlights	Deadlines to Consider	Additional Details
Advanced Energy Project Credit (48C)	Extends the 30% investment tax credit to clean energy projects to strengthen domestic energy manufacturing and support the production and recycling of clean energy products. It also expands to include projects at manufacturing facilities that want to reduce their GHG emissions by at least 20%.	Effective January 1, 2023	- Tax credit is funded at $10 billion for eligible projects. - Can be applied to low-carbon industrial heat, carbon capture, transport, utilization and storage systems, and equipment for recycling, waste reduction, and energy efficiency.

Inflation Reduction Act: Clean Energy Production Tax Credits

	Highlights	Deadlines to Consider	Additional Details
Extension of Renewable Electricity Production Tax Credit (Section 45)	Extends the existing production tax credit for applicable renewable energy sources. This tech-specific PTC ends in **2024** and is replaced by the new tech-neutral Clean Electricity PTC (45Y) which begins in **2025**.	Extends the date of construction for geothermal, wind, closed- and open-loop biomass, landfill gas, municipal solid waste, hydropower, and marine and hydrokinetic facilities to **2024**.	Increases hydropower, municipal solid waste, and marine and hydrokinetic credit to full value (was previously halved). Strikes the offshore wind credit phaseout for facilities placed into service before 2022.
New Clean Electricity Production Tax Credit (45Y)	This newly established, tech-neutral PTC replaces the Renewable Electricity Production Tax Credit once it phases out at the end of 2024. 45Y is an emissions-based incentive that is neutral and flexible between clean electricity technologies. Taxpayers choose between a PTC (45Y) and an ITC (48D).	Credits are set to phase out the later of 2032 or when emission targets are achieved (i.e., the electric power sector emits 75% less carbon than 2022 levels). Facilities will be able to claim a credit at 100% value in the first year, then 75%, then 50%, and then 0%.	Creates a PTC credit of 1.5 cents per kWh of electricity produced and sold or stored at facilities placed into service after 2024 with zero or negative GHG emissions. Facilities may use carbon capture, utilization, and storage (CCUS) to reach qualifying emissions levels.

Inflation Reduction Act: Community Investment and Energy Justice

	Highlights	Additional Details
Neighborhood Access and Equity Grants	**$3 billion**, with **$1.1 billion** set aside for disadvantaged communities, to the FHA	. Grants to improve transportation access and mitigate negative safety or environmental impacts in underserved communities. Grants may be used for improvements to reduce air pollution and GHG emissions, manage stormwater run-off, address urban heat islands, and to monitor air quality, transportation related GHG emissions and pollution, and gaps in tree canopy coverage. State, local, territory, and Tribal government entities are eligible. Federal cost share of a project in a disadvantaged or underserved community may be up to 100%.
Energy Credit for Solar and Wind in Low-Income Communities	Creates a **40% investment tax credit** for solar or wind projects; 20% in certain scenarios	Creates a 40% investment tax credit for solar or wind projects located in a low-income community or on Tribal land 20% for facilities part of low-income residential housing or low-income economic benefit projects.

Inflation Reduction Act: Focus on Investment Tax Credit

- IRC Section 48 outlines investment for certain energy-related property (”ITC”).
- The ITC was extended by IRA – IRA extended date of construction to 2024 in most cases.
  - Maintains a 30% credit for solar energy property
  - Current ITC (which is tech specific) will be replaced by the new tech-neutral Clean Electricity (which begins in 2025)
- To claim the ITC, taxpayer should file **Form 3468**.
- All three of the Clean Energy Investment Tax Credits include **direct pay** and **transferability** (as well as all Clean Energy Production Credits elaborated on later slides).

Inflation Reduction Act: What is Direct Pay?

- Direct pay allows a taxpayer to **treat tax credits that it has earned as an overpayment of taxes**.
- This allows the taxpayer to utilize the **tax refund mechanism** in the tax code to receive a direct payment of cash from the Treasury Department in lieu of monetizing the tax credit by other means.
- Provides opportunities for exempt **organizations** to utilize these tax credits where, previously, these organizations would not have benefited.
- In a nutshell – Potential GAMECHANGER.

Inflation Reduction Act: What is Transferability?

- "**Transferable Tax Credits**" mean that taxpayers can sell all or part of their tax credits to an unrelated party.
  - Note, transferability is **NOT** an option for the Tax-Exempt Organizations.
- **Transferability Requirements**:
  - The sale must be for cash.
  - The is a 20 percent penalty if the claimed credit exceeds what the project was entitled to.
  - The proceeds would be exempt from income but not deductible to the buyer.
- **What Happens After I Transfer a Credit?**
  - Once a credit is transferred, the transferee cannot transfer it further.
  - Also, credits which have been carried forward may not be transferred.

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Making Clean Energy and Microgrids a Reality for Tax-Exempt Organizations

- Tax-exempt organizations usually cannot benefit from tax credits (as they don't owe any taxes which could be offset by said tax credit).
- Now, because of direct pay, exempt organizations can benefit.
- Also, relaxation of tax credit haircut for use of tax-exempt financing – haircut now capped at 15%.
- Note, Tax-Exempt Organizations still not able to take advantage of the accelerated depreciation.

The New Question – What Tax Credit Program Do You Want To Use?

- Given the expansion of both the ITC and PTC, all entities, including Tax Exempt Organizations need to assess whether to take:
  - The One-Time ITC credit, or
  - The On-going (10-year) PTC credit.
- The next few slides provide some examples of this assessment.

Example – PTC vs ITC

BASIC ASSUMPTIONS

EXAMPLE			
Cost	3,000,000		
Output	2,000	MwH	
Percent ITC	95%		
Diverted costs	10	centes per KwH	
energy inflation	5%		

Example – PTC vs ITC 40%

ITC at 40%										
Cost	3,000,000									
ITC at 40%	(1,140,000)	30% plus OZ 10%								
Net cost	1,860,000									
	1	2	3	4	5	6	7	8		
Revenue	200,000	210,000	220,500	231,525	243,101	255,256	268,019	281,420		
ROI (Cost less ITC)	11%	11%	12%	12%	13%	14%	14%	15%		
Break-even	7 years 10 months							(49,822)		
PTC										
	1	2	3	4	5	6	7	8	9	10
Revenue	200,000	210,000	220,500	231,525	243,101	255,256	268,019	281,420	295,491	310,266
PTC	55,000	55,000	55,000	55,000	55,000	55,000	55,000	55,000	55,000	55,000
	255,000	265,000	275,500	286,525	298,101	310,256	323,019	336,420	350,491	365,266
ROI (full cost)	9%	9%	9%	10%	10%	10%	11%	11%	12%	12%
Break-even	9 years 8 months									(65,579)

Example – PTC vs ITC 30%

ITC at 30%										
Cost	3,000,000									
ITC at 30%	(855,000)	30%								
Net cost	2,145,000									
	1	2	3	4	5	6	7	8	9	
Revenue	200,000	210,000	220,500	231,525	243,101	255,256	268,019	281,420	295,491	
ROI (Cost less ITC)	9%	10%	10%	11%	11%	12%	12%	13%	14%	
Break-even	8 years 9 months								(60,313)	
PTC										
	1	2	3	4	5	6	7	8	9	10
Revenue	200,000	210,000	220,500	231,525	243,101	255,256	268,019	281,420	295,491	310,266
PTC	55,000	55,000	55,000	55,000	55,000	55,000	55,000	55,000	55,000	55,000
	255,000	265,000	275,500	286,525	298,101	310,256	323,019	336,420	350,491	365,266
ROI (full cost)	9%	9%	9%	10%	10%	10%	11%	11%	12%	12%
Break-even	9 years 8 months									(65,579)

What Hasn't Changed?

- If expending capital is a concern for a Tax-Exempt Organization, the models discussed at the beginning are still available.
  - Treat clean energy project as an expense, rather than a capital expenditure
- PPA Structure – Tax-Exempt Organization only pays for what it takes.
  - No capital expenditure
  - No O&M costs
  - Performance risk on system owner, i.e., bad weather risk
  - System owner may be able to more efficiently utilize all available tax benefits
- Service Agreement Structure – Tax-Exempt Organizations makes a set payment for provision of services.
  - Similar benefits for PPA analysis
- Pre-August 2022 options, but potentially more attractive after tax credit expansion and adders.

What's next?

- Guidance on "wages" and "internships"

Questions and comments?

Thank You!

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