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## New Guidance on Energy Community Bonus U.S. Tax Credit

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The U.S. Inflation Reduction Act of 2022 (the “IRA”) provides clean energy bonus tax credit incentives to help communities near brownfield sites or that historically depended on fossil fuel-based industries. These include communities that have proximity to retired or closing coal power plants and coal mines. The IRA’s provisions are intended to spur investment and jobs in these communities from new clean energy projects.

On April 4, 2023, the IRS released a Notice of Proposed Rulemaking (the “Notice”) regarding the bonus tax credits for investments in these “energy communities.” Until issuance of the forthcoming proposed regulations, taxpayers can rely on the rules outlined in the Notice.

### Background

With respect to 26 U.S. Code § 45 or 45Y clean electricity production tax credits (“PTC”) and § 48 or 48E clean electricity investment tax credits (“ITC”) under the IRA, eligible facilities located in or placed in service within an “energy community” are eligible for increased credit amounts or rates.<sup>1</sup> More specifically, the PTC rate is increased by 10%, and the ITC rate is increased by 10 percentage points (or two percentage points if the facility is subject to and does not satisfy a separate prevailing wage and apprenticeship requirement).<sup>2</sup> Qualified facilities can include solar farms, wind farms, nuclear power plants, hydrogen electrolyzers, and energy storage facilities.

Under the definitions included in the IRA and clarified by the Notice, an energy community is any one of the following:<sup>3</sup>

- **Coal Closure Category** – A census tract containing coal-fired electric generating units that have retired since December 31, 2009, or coal mines that have closed since December 31, 1999, or census tracts directly adjoining such census tracts;
- **Statistical Area Category** – A metropolitan statistical area (“MSA”) and non-metropolitan statistical area (“non-MSA”) that either (i) has, or had at any time after December 31, 2009, 0.17% or greater direct employment or 25% or greater local tax revenues related to the extraction, processing, transport, or storage of fossil fuels (coal, oil, or natural gas), and (ii) has an unemployment rate higher than the national average for the previous year as determined by the Treasury Secretary; or

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- **Brownfield Category** – A brownfield site as defined under the Comprehensive Environmental Response, Compensation, and Liability Act (“CERCLA” or Superfund).

### Coal Closure Category

The Notice elaborates on the categories of closed coal mines and retired coal-fired electric generating units with reference to data maintained by the U.S. Mine Safety and Health Administration (MSHA) and Energy Information Administration (EIA), respectively. The Notice also clarifies that census tracts are “directly adjoining” if the boundaries touch at any single point.<sup>4</sup>

### Statistical Area Category

The Notice provides definitions of MSAs and non-MSAs, as well as standards for measuring the applicable area’s direct employment and unemployment rate. The Notice does not provide guidance on the fossil fuel-related tax revenue for an MSA or non-MSA and instead solicits public comments addressing the possible data sources, revenue categories, and procedures.<sup>5</sup>

MSAs and non-MSAs. MSAs are grouped according to standards determined every 10 years by the Office of Management and Budget (OMB). Non-MSAs are generally nonmetropolitan areas as determined by the Occupational Employment and Wages Statistics division of the U.S. Bureau of Labor Statistics (BLS). MSAs are first delineated, and then counties outside of MSAs are grouped together as nonmetropolitan areas. [Appendix A](#) to the Notice identifies all potentially relevant MSAs and non-MSAs that may qualify.

**Direct employment.** The fossil fuel direct employment level in an MSA or non-MSA is determined by dividing (A) the number of people employed in the industries identified in the 2017 North American Industry Classification System (including oil and gas extraction, coal mining, drilling oil and gas wells, support activities and pipeline transportation), by (B) the total number of people employed in that area. [Appendix B](#) to the Notice identifies specific MSAs and non-MSAs that satisfy the fossil fuel employment threshold.

**Unemployment rate.** The unemployment rate in an MSA or a non-MSA is determined using the Local Area Unemployment Statistics annual data published by the BLS, dividing the total number of unemployed individuals within the MSA or non-MSA by the total labor force in such area.

Recognizing the lag in availability of annual county employment rates for a calendar year, which generally are released in April of the following calendar year, the Treasury Department and the IRS intend to update the listing of the MSAs and non-MSAs satisfying the fossil fuel industry employment standard each May. For example, the energy communities defined by the 2022 unemployment rates will be designated in May of 2023 and will remain effective until the next update in May 2024.

### Brownfield Category

The IRA uses the CERCLA definition of a “brownfield site” which is “real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant” and “mine-scarred” land.<sup>6</sup>

Additionally, the Notice provides a safe harbor under which a site will be considered an energy community if it fits within any of the following three categories:

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- The site was previously assessed through federal, state, territory, or federally recognized Indian tribal brownfield resources as meeting the definition of a brownfield site under CERCLA.
- An ASTM E1903 Phase II Environment Site Assessment has been completed with respect to the site and confirms the presence on the site of a hazardous substance or a pollutant or contaminate.
- For a project with a nameplate capacity of not greater than 5MW (AC), an ASTM E1527 Phase I Environmental Site Assessment has been completed.

### Location Requirement

The Notice clarifies that a project must either have 50% or more of its nameplate capacity in an energy community or have 50% or more of its square footage in an energy community.<sup>7</sup> Additionally, for purposes of the PTC, whether a qualified facility is located in an energy community is determined separately for each taxable year of the qualified facility's 10-year credit period, and for purposes of the ITC, whether an energy project is placed in service in an energy community is determined as of the placed-in-service date.<sup>8</sup> As a result, projects seeking the PTC in a Statistical Area Category, may lose or gain eligibility during the life of the project if the local unemployment rate drops below or rises above the national average. However, the Notice sets forth a safe harbor, providing that if a taxpayer begins construction after December 31, 2022 in a location that is an energy community as of the beginning of construction date, then, with respect to that facility, the location will continue to be considered an energy community for the entire 10-year credit period for the PTC or on the placed-in-service date for the ITC.

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### ENDNOTES

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- <sup>1</sup> In addition, under 26 U.S. Code § 48C(e) (the Advanced Energy Project Credit), \$4 billion of the total \$10 billion in tax credits must be allocated to projects located in energy communities. See [S&C Energy Transition Insights: New Guidance on \\$10 Billion Worth of Advanced Energy Project Tax Credits](#).
  - <sup>2</sup> §§ 45(b)(11); 45Y(g)(7); 48(a)(14); 48E(a)(3)(A).
  - <sup>3</sup> § 45(b)(11)(B).
  - <sup>4</sup> Notice § 3.04.
  - <sup>5</sup> Notice § 3.03.
  - <sup>6</sup> 42 U.S.C. § 9601(39)(A); 42 U.S.C. § 9601(39)(D)(ii)(III); Notice § 3.02. CERLA's definition excludes certain specific categories from the definition of "brownfield site," such as property subject to administrative actions or judicial orders under the Solid Waste Disposal Act. 42 U.S.C. § 9601(39)(B)
  - <sup>7</sup> Notice § 4.02.
  - <sup>8</sup> Notice § 4.01.

Questions regarding the matters discussed in this publication may be directed to [Isaac Wheeler](#), [Inosi Nyatta](#), [Sam Saunders](#) or any Sullivan & Cromwell LLP lawyer with whom you have consulted in the past on similar matters. Additional S&C resources about energy transition matters may be found [here](#).

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