February 21, 2023

New Guidance on $10 Billion Worth of Advanced Energy Project Tax Credits

The Inflation Reduction Act of 2022 (the "IRA") provides for, among many other credits, up to $10 billion in investment tax credits to be allocated to qualifying advanced energy projects (the Advanced Energy Project Credit, Section 48C(e) of the Internal Revenue Code). "Qualifying advanced energy projects" include projects that re-equip, expand, or establish a facility for the production or recycling of clean energy equipment or vehicles or for the processing, refining or recycling of critical minerals, or that re-equip a facility with equipment designed to reduce greenhouse gas emissions by at least 20%.[1]

The amount of the credit equals 30% of the qualified investment, provided prevailing wage and apprenticeship requirements are met,[2] or 6% if not.[3] $4 billion of these credits must be allocated to projects located in certain "energy communities."[4] Taxpayers must complete an application process involving the Department of Energy ("DOE") and Internal Revenue Service ("IRS") in order to claim the credit.[5] The IRS issued its first guidance on implementing the Advanced Energy Project Credit program on February 13, 2023 in Notice 2023-18.

Key Considerations for the Advanced Energy Project Credit

Manufacturers, industrial companies, project developers and potential investors and tax credit purchasers should take note of the following:

- **Credit is transferable for cash and, for tax exempt entities, refundable**. Similar to most other IRA credits, the Advanced Energy Project Credit may be transferred for cash to another taxpayer (but once transferred, cannot be re-transferred). This means project owners with insufficient tax liabilities can more easily monetize the tax credit and do not necessarily need to employ complex tax equity structures. Credit transferability and refundability also offer the potential for new investors and other supporters of projects to participate via the offtake of tax credits.
- **Credit is not stackable**. Unlike some other IRA credits, the Advanced Energy Project Credit generally cannot be combined with other credits. Taxpayers are not eligible for the credit if the project is eligible for the Section 48 investment tax credit (ITC), advanced coal project credit (48A), gasification project credit (48B), clean electricity investment credit (48E), carbon oxide sequestration credit (45Q) or clean hydrogen production credit (45V). Also, facilities producing solar energy, wind energy, inverter, qualifying battery, and applicable critical mineral manufactured components are not eligible for the advanced manufacturing credit (45X) if the facility has claimed the Advanced Energy Project Credit.

Project sponsors will need to analyze whether taking this credit is the best choice compared to utilization of other credits.

- **First deadline for applications is July 31, 2023 and projects must generally be placed in service within four years of credit allocation**. At least two rounds of credit allocation will be conducted. The IRS anticipates allocating $4 billion of the $10 billion in Round 1 in accordance with the below timeline. The timing of Round 2 is still to be determined.
  - To be considered for Round 1, a concept paper must be submitted to DOE by July 31, 2023. Once DOE reviews the concept paper, DOE will respond to the taxpayer with a letter encouraging or discouraging the submission of an application.
  - Applications must then be submitted by a yet to-be-determined date (additional IRS guidance is expected by May 31, 2023). DOE will then review each application and rank recommended projects for the IRS to accept or reject.
  - Within two years of receiving an IRS acceptance letter, the taxpayer must notify DOE that the certification requirements (generally involving evidence that the taxpayer has met all requirements to commence construction of the project) have been met. If the certification requirements are met, the IRS will then send a certification letter to the taxpayer, who must place the project in service within two years thereafter. Failure to meet these deadlines will result in forfeiture of the allocated credits.
- **DOE will consider technical and policy factors in its credit allocation recommendations**. Additional guidance will be issued on the DOE technical review criteria, which is anticipated to include assessment of net GHG emission avoidance or reduction, job creation and other community benefits. DOE may also consider one or more policy factors, including giving priority to projects not eligible for support from other DOE programs (such as DOE loan guarantees) and projects that address specific gaps, vulnerabilities or risks in the domestic production of clean energy products. Timing of DOE review within development and transaction timelines will be important to understand.
- **Significant changes in project plans post-application will void the credit**. If plans for the project change in any significant respect from those set forth in the concept paper and the application, the taxpayer must inform DOE and the IRS and the credit application or allocated credits will be voided. A “significant change” is “any change that a reasonable person would conclude might have influenced DOE in recommending or ranking the project or the IRS in issuing the Allocation Letter ….” Moving the project to a different census tract is given as an example of a significant change.

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ENDNOTES

[1] IRC § 48C(c)(1)(A). Such qualifying projects do not include any portion for the production of property that is used in the refining or blending of transportation fuels (other than renewable fuels). IRC § 48C(c)(1)(B).

[2] IRC § 48C(e)(4)(B).

[3] IRC § 48C(e)(4)(A).

[4] IRC § 48C(e)(2). “Energy communities” generally include census tracts with retired coal mines or retired coal-fired electric generating units, along with any adjacent census tracts. IRC § 45(b)(11)(B)(iii).

[5] IRC § 48C(e)(3)(A).

Questions regarding the matters discussed in this publication may be directed to Isaac Wheeler, Co-Head of Tax and Inosi Nyatta, Co-Head of Project Development & Finance, or to 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.