EXCERPT

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Effect of Looming Technology-Neutral ITC, PTC Varies, Depending on Perspective

BRAD STANHOPE, SENIOR EDITOR, NOVOGRADAC

When the clean energy investment tax credit (ITC) and production tax credit (PTC) switch to technology-neutral status in January 2025, it will either be a game-changer or more of the same, depending on your perspective.

For traditional wind (PTC) and solar (ITC) developers, there won't be much change. But for other technologies?

"I think it's hugely significant because it does a few things," said Scott Cockerham, a partner at Latham & Watkins LLP, who works extensively in the clean energy space. "One is that it's tech-neutral in the sense that your asset can technically be *anything* as long as it's creating electricity and results in zero greenhouse gases."

Cockerham said that has significance going forward.

"What's interesting is that you could [someday] get tax credits for assets that haven't been invented yet, so there's a lot of potential there," he said. "In the older code section, the qualification was set, down to what it was on the component level. If you had a new technology that isn't included, you'd have to lobby Congress to get it added [to be eligible]. This is more nuanced and takes future innovation into account."

Bryen Alperin, partner and managing director at investor/syndicator Foss and Co., said many current participants in the clean energy world won't see much of a difference, presuming the regulations don't include any dramatic shifts.

How the Change Works

One of the many provisions of the Inflation Reduction Act (IRA) of 2022 moves the ITC and PTC to tech-neutral status in 2025, with a sunset date of 2032 or later (depending on overall emissions totals). The Internal Revenue Service issued proposed guidance for the credits in June that included a list of technologies that automatically qualify for the credits: solar, wind, hydropower, geothermal, marine and hydrokinetic, nuclear and certain waste energy recovery properties, along with energy storage. The guidance also created a pathway for other technologies to qualify, including that a facility must both generate electricity and have an anticipated greenhouse gas emissions rate that is zero or negative. The applicant will have to prove the zero-emissions rate if the technology isn't on the automatic list.

The proposed guidance declares projects that begin construction in 2024 are eligible for both the existing credits and the tech-neutral credits. Cockerham and Alperin each expect many developers to choose the current credits.

Changes from Existing ITC, PTC

For technologies that don't automatically qualify for the tech-neutral credits, establishing zero emissions will be the key and Alperin said it may not be simple.

"A key difference between these tech-neutral credits and the traditional ITC and PTC lies in the emissions requirements and the process for demonstrating compliance," he said. "Will there be a specific agency responsible for certifying compliance and will it have adequate funding? This could introduce delays if the approval process is not well defined."

He said other provisions of the IRA have had unexpected complications.

"The way the low-income adder was implemented, you have to apply after a property is placed in service," Alperin said. "If there's something similarly challenging that for emissions compliance, it may limit some projects' ability to raise financing, so there's some risk in the uncertainty around how this guidance might be written."

There's also a question of the definition of "zero emissions"–an issue that may be addressed in final regulations.

"You might still emit greenhouse gases, but if you are capturing carbon simultaneously, you could achieve net-zero emissions. The question is what would need to be done to still meet the standards?" Alperin said. He added that renewable natural gas, biomass and other clean fuel technologies could face challenges in meeting the zero-emission threshold, depending on how the guidelines are defined.

On the other hand, Cockerham said things won't change much for traditional solar and wind developers.

"One thing that's helpful is that wind and solar are on the list of technologies that automatically qualify," Cockerham said. "If you have a technology that's not on that list, you have to get a lifecycle analysis [for emissions] so it's much more complicated. But since solar and wind automatically qualify, for the most part it will be business as usual."

Final Guidance Crucial

Cockerham said solar developers are awaiting final guidance on the ability to aggregate ITC-eligible facilities that have common characteristics. The proposed guidance does not include aggregation, which has major implications regarding the ability to qualify for bonuses such as prevailing wage and apprenticeship, domestic content, energy communities and other IRA bonuses.

Alperin said he's optimistic that the guidance will come soon.

"We expect to see guidance this year," said Alperin. "Hopefully, it will be something we can work with. There seems to be enough runway to address any challenges that arise."

Cockerham also said he wouldn't be surprised if the final regulations come out before the end of 2024, partly due to the normal pace of regulations and partly that President Joe Biden's administration may want to issue guidance before a potential transition of power in January.

Potential for Future Technology

Perhaps the biggest impact will come as new technologies are created and become eligible for the ITC and PTC.

"Consider that in the next five to 10 years, we may develop new types of fusion or other energy technologies that don't exist today," said Alperin. "Once they meet the emissions criteria, those technologies could qualify for the credits without waiting for a legislative amendment to the tax code."

However, Cockerham said it won't be a simple task to qualify for the new tech-neutral credits.

"I think it will be much more challenging for any type of project that's not on this list," Cockerham said. "A fuel cell currently qualifies under Section 48, but it's not clear how that would qualify under a zero-emissions lifecycle analysis. To the extent that assets are outside this list, the challenge is that investors are not used to looking into this with an engineering analysis for emissions, so I could see them be a little nervous about dipping their toes into it."

Future Impact Uncertain

Alperin said that many traditional solar and wind developers and investors are not focused on the change.

"Often, industries operate in silos without considering other tax credits," Alperin said. "For example, solar and wind developers may not focus on carbon capture or clean hydrogen. This shift could bring new technologies into the mix beyond traditional renewables. As tax credit investors, we're usually technology-agnostic, so if the market grows from $20 billion to $80 billion in credits due to growth of new technologies, it might become more challenging for solar or wind developers to secure the tax equity they need."

Alperin said that investors are probably not as affected as developers.

"From an investor perspective, these credits are almost identical to the existing ones," Alperin said. "Active investors will likely see them as the same credit, with a few additional requirements. Will the fact that it's technically a different credit create challenges for securing investor approval? My guess is that, given the similarities, it won't be a significant issue, but investors will need to be comfortable with the new requirements. Tax insurance might play a role, as it has already addressed some ambiguities under the IRA. It could also be useful for emerging technologies."

Future guidance, however, could change things.

"When considering a future presidential administration attempting to scale back the Inflation Reduction Act provisions, one approach might be through adjustments in how the guidance is written or revised," Alperin said. "An obvious target could be the implementation of the tech-neutral credits."

But entering the final quarter of 2024, the change to tech-neutral credits is generally good news.

"This extends the runway pretty significantly for the credits," Cockerham said. "They were temporary and had to be extended over and over. These are set to go on until 2032 at the earliest. They may phase down after that, depending on the level of greenhouse gas emissions compared to when the IRA passed. That could go on a long time." ❖

NOVOGRADAC®

CONTACT

CORRESPONDENCE AND EDITORIAL SUBMISSIONS
Teresa Garcia
teresa.garcia@novoco.com
925.949.4232

ADVERTISING INQUIRIES
Christianna Cohen
christianna.cohen@novoco.com
925.949.4216

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