

Insights

IRS GUIDANCE ON ENERGY COMMUNITY PTC AND ITC BONUS CREDITS PROVIDES SOME NEEDED CLARITY

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On April 4, 2023, the Internal Revenue Service (the “**IRS**”) and the Department of the Treasury (the “**Treasury**”) issued Notice 2023-29 (the “**Notice**”) announcing an intention to propose regulations, and providing interim guidance, with respect to the requirements that taxpayers must satisfy in order to be eligible for the “energy community” bonus credit added by the Inflation Reduction Act of 2022 (“**IRA**”) to the production tax credit (“**PTC**”) under section 45^[1] (and, beginning in 2025, section 45Y) and the investment tax credit (“**ITC**”) under section 48 (and, beginning in 2025, section 48E).

The Notice recognizes the need to provide clarity to developers and investors with respect to the requirements for qualifying for the energy community bonus credit, by specifying the criteria to be used to determine whether a project is in an energy community and, where possible, identifying the information that can be used to establish that a project qualifies for the bonus credit. The Notice also provides taxpayer-friendly rules that can be used to confirm that a project satisfies the location requirements.

The Notice describes forthcoming proposed regulations with rules for governing whether a community constitutes an energy community, as well as whether a qualified facility, energy project, or energy storage technology is located within an energy community. The proposed regulations will apply to taxable years ending after April 4, 2023, and taxpayers may rely upon the Notice until issuance of the proposed regulations.

On June 15, 2023, the IRS and the Treasury issued additional notices, Notices 2023-45 (“**Notice 2023-45**”) and 2023-47 (“**Notice 2023-47**”) (Notice 2023-45 and Notice 2023-47, collectively, with the Notice, the “**Notices**”), clarifying the requirements for projects and facilities to qualify for the bonus credit, both discussed in further detail below.

BACKGROUND

The IRA provides increased PTC amounts for projects *located in* an “energy community,” and also provides increased ITC amounts for projects that are *placed in service* within an energy

community. Generally, the PTC bonus credit for projects satisfying the energy community requirements is 10% of the PTC otherwise available, and the ITC bonus credit for projects satisfying the energy community requirements is ten percentage points or (two percentage points if the prevailing wage and apprenticeship requirements are not satisfied with respect to project).

The IRA established three categories of geographic areas that may qualify as an “energy community” eligible for the increased PTC and ITC:

- brownfield sites, as defined in subparagraphs (A), (B), and (D)(ii)(III) of Section 101(39) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (“CERCLA”) (the “**Brownfield Category**”),
- a metropolitan statistical area (“**MSA**”) or non-metropolitan statistical area (“**non-MSA**”) which (i) has, or at any time during the period beginning after December 31, 2009, had, either 0.17% or greater direct employment related to the extraction, processing, transport or storage of coal, oil or natural gas (referred to below as the “fossil fuel industries”), or 25% or greater local tax revenues related to the fossil fuel industries, and (ii) has higher than average unemployment rates (the “**Statistical Area Category**”), and
- a census tract in which there is located either (i) a coal mine that has had, since December 31, 1999, a status of abandoned or sealed, or (ii) a coal-fired power generating unit that has been classified, after December 31, 2009, retired, or any adjoining census tract (the “**Coal Closure Category**”).

ENERGY COMMUNITIES

The Notice provides additional detail for determining whether a particular location is within one of three categories of energy communities.

BROWNFIELD CATEGORY

For purposes of the Brownfield Category, a brownfield site is defined in § 101(39)(A), (B), and (D)(ii)(III) of CERCLA as real property, the expansion, redevelopment, or reuse of which may be complicated by the presence of potential presence of a hazardous substance, pollutant, or contaminant and certain mine-scarred land. A brownfield site does not include categories of property described in Section § 9601 (39)(B) of CERCLA.

- The Notice includes a safe harbor provision under which a site will meet the definition of a brownfield site, if one of the following are satisfied:
 - Previously, the site was assessed through federal, state, territory, or federally recognized Indian tribal brownfield resources as meeting the definitional requirements of a brownfield site under 42 U.S.C. § 9601(39)(A). The Notice identifies places to find potential lists of sites that have been assessed in this manner.

- The site contains the presence of a hazardous substance as defined under 42 U.S.C. § 9601(14), or a pollutant or contaminant as defined under 42 U.S.C. § 9601(33), as confirmed by an ASTM E1903 Phase II Environmental Site Assessment.
- For a site with a project with a nameplate capacity of not greater than 5MW (AC), an ASTM E1527 Phase I Environmental Site Assessment has been performed and such ASTM E1527 Phase I Environmental Site Assessment has identified the presence or potential presence of a hazardous substance as defined under 42 U.S.C. § 9601(14), or a pollutant or contaminant as defined under 42 U.S.C. § 9601(33), as clarified by Notice 2023-45.

STATISTICAL AREA CATEGORY

An MSA or non-MSA is within the Statistical Area Category if it (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 fossil fuel industries, and (ii) has an unemployment rate at or above the national average unemployment rate for the previous year.

- The Notice summarizes how MSAs and non-MSAs are determined and identifies sources of information for identifying MSAs and non-MSAs. Generally, MSAs are defined according to standards that are determined by the Office of Management and Budget every 10 years, and non-MSAs are determined by the Bureau of Labor Statistics in conjunction with individual states. Appendix A to the Notice delineates the MSAs and non-MSAs for purposes of the Notice.
- For the purposes of determining whether an MSA or non-MSA has 0.17% or greater direct employment related to the fossil fuel industries, the Notice identifies the industries (based upon 2017 NAICS codes) that are to be taken into account, and also identifies the source of Census Bureau information to be used in determining for the MSA or non-MSA, as applicable, the number of employees in those industries and the total number of employees. Appendix B to the Notice lists the MSAs and non-MSAs that have, or since December 31, 2009 have had, 0.17% or greater employment in the fossil fuel industries.
- The Notice acknowledges that there are challenges in determining whether an area qualifies under the Statistical Area Category based upon fossil fuel tax revenue, due to the lack of publically available data, and due to the fact that a given MSA or non-MSA may include multiple taxing jurisdictions. Accordingly, the Notice does not specify how fossil fuel tax revenue is to be determined, but invites public comments addressing possible data sources, revenue categories and procedures to determine whether an MSA or non-MSA has 25% or greater local tax revenues related to the fossil fuel industries.
- The Notice specifies how the unemployment rate for an MSA or non-MSA will be determined based upon Local Area Unemployment Statistics annual data for counties from the Bureau of

Labor Statistics. The Notice also provides that Treasury and the IRS intend to issue annual lists, generally in May of each year, of the MSAs and non-MSAs that qualify under the Statistical Category based upon the employment data from the prior year.

- Appendix 1 of Notice 2023-47 (“**Appendix 1**”) lists additional MSAs and non-MSAs that have, or since December 31, 2009 have had, 0.17% or greater employment in the fossil fuel industries based on the 2021 County Files of the County Business Patterns, as published by the Census Bureau. Appendix 1 should be used in conjunction with Appendix B of the Notice to determine MSAs and non-MSAs that have, or since December 31, 2009 have had, 0.17% or greater employment in the fossil fuel industries.
- Appendix 2 of Notice 2023-47 (“**Appendix 2**”) lists additional MSAs and non-MSAs that have, or since December 31, 2009 have had, 0.17% or greater employment in the fossil fuel industries and have an unemployment rate at or above the national average unemployment rate for calendar year 2022. Appendix 2 uses the County Files of the County Business Patterns, as published by the Census Bureau, for years 2010 through 2021, and 2022 calendar year county unemployment rates released on April 21, 2023, by the Local Area Unemployment Statistics program of the Bureau of Labor Statistics.
- Notice 2023-47 states additional guidance identifying MSAs and non-MSAs will generally be published in May of each year.

COAL CLOSURE CATEGORY

Under the IRA, the Coal Closure Category includes a census tract (or a census tract directly adjoining such census tract), in which either (i) a coal mine has closed after December 31, 1999, or (ii) a coal-fired electric generating unit has been retired after December 31, 2009.

- For purposes of the Coal Closure Category, the Notice adopts the definition and delineation of census tracts used by the Census Bureau for purposes of the 2020 Decennial Census.
- The Notice provides that a closed coal mine is a coal mine classified as a surface or underground mine that has had at any point in time, since December 31, 1999, a status of abandoned or abandoned and sealed by the U.S. Department of Labor’s Mine Safety and Health Administration (“MSHA”) in the Mine Data Retrieval System (“MDRS”). The category does not include mines that have irregular location information in the MDRS listing, but provides that taxpayers may submit to MSHA information to correct the listing.
- A retired coal-fired electric generating unit is an electric generating unit classified as retired at any time since December 31, 2009, by the U.S. Energy Information Administration (“EIA”) of the U.S. Department of Energy in the Preliminary Monthly Electric Generator Inventory or the Electric Generator Inventory. The Notice specifies the EIA reporting information that can be used to determine the status of a particular generator unit. Generator units with irregular

location information are excluded, but taxpayers may submit to EIA information to correct the listing. Appendix C to the Notice lists census tracts falling under the Coal Closure Category.

- Census tracts are considered directly adjoining if their boundaries touch at any single point.
- Appendix 3 of Notice 2023-47 (“**Appendix 3**”) lists census tracts falling under the Coal Closure Category based upon data from the MHSA’s MDRS and the EIA’s Forms 860 and 860M as of May 1, 2023. Appendix 3’s list of census tract is also informed by the historical extracts from the MHSA’s MDRS which states each status change for a mine.
- Notice 2023-47 states additional guidance identifying census tracts falling under the Coal Closure Category will generally be published in May of each year.

Located in and Placed in Service Tests

Under the IRA, a project can qualify for the PTC bonus credit only if the project is *located in* an energy community, and a project can qualify for the ITC bonus credit only if the project is *placed in service* in an energy community. The Notice provides additional clarity on how these tests are to be applied. In addition, the Notice addresses three important issues relating to determining whether a project is located in, or placed in service in, an energy community. First, the Notice recognizes the need to facilitate the process of financing a project by providing relative certainty concerning whether a location is in an energy community, and provides a taxpayer-friendly rule to address possible changes in the status of a particular location following commencement of construction. Second, the Notice provides clearer rules for applying the energy community rules to project that is partially, but not entirely, located within an energy community. Finally, the Notice addresses the possible consequences if there are changes to the project configuration in a year (i.e., if a portion of a project is damaged or removed from operation).

Generally, for the purposes of the PTC, whether the project is *located in* an energy community is determined separately for each year of the 10 year credit period, and for any taxable year the location requirement is satisfied if the project is located in an energy community during any part of the taxable year.

For purposes of the ITC, whether a project is *placed in service* in an energy community determined as of the placed-in-service date, i.e., the date the ITC is determined.

The Notice recognizes that the status of a particular location could change over time (i.e. due to a change in the unemployment rate). The resulting uncertainty could make it difficult to rely on the bonus credits as the basis for the fully committed capital needed to finance a project. The Notice addresses this by providing that, if a taxpayer begins construction of a project in a location that is determined to be an energy community as of the beginning of construction date, then the location will be considered to be an energy community for the duration of the 10-year credit period for the PTC, and through the placed-in-service date for the ITC.^[2] To determine the start of construction

date, the Notice adopts the rules spelled out in the IRS notices initially issued in connection the pre-IRA PTC and ITC phase-out provisions, and more recently adopted in connection with the prevailing wage and apprenticeship requirements.^[3] Existing challenges faced by developers in complying with the start of construction requirements, including satisfying the continuity requirements, remain unresolved.

For projects that are located in part, but not entirely, within an energy community, the Notice provides that the project is “located in” or “placed in service within” an energy community for purposes of the bonus credits under the following rules:

NAMEPLATE CAPACITY TEST

A project is considered located in or placed in service within an energy community if 50% or more of the project’s nameplate capacity is in an area that qualifies as an energy community. The portion of a project’s nameplate capacity attributable to the energy community is determined by dividing the nameplate capacity of the project’s energy-generating units that are located in an energy community by the total nameplate capacity of all the energy-generating units of the project. For offshore projects where none of the generating units are located in a census tract, the Notice attributes the nameplate capacity to the location of the land-based conditioning equipment that is closest to the interconnection point.

FOOTPRINT TEST

If a project does not have nameplate capacity, the project is treated as located in or placed in service within an energy community if 50% or more of its square footage is in an area that qualifies as an energy community. The percentage is determined by dividing the square footage of the project located in an energy community by the total square footage of the project.

Overall, the Notices facilitates the ability of project developers to secure the potential tax credit equity attributable to the energy community bonus credit, to supplement the project’s capital stack, by providing clarity on a number of issues. These include the Brownfield Category safe harbor, the sources of information to confirm the status and characteristics of MSAs and non-MSAs, whether a location qualifies within the Coal Closure Category, and the effect of changes in the characteristics of an area over time. Some areas of uncertainty remain, including principally how to determine the fossil fuel-related tax revenue of an MSA or non-MSA, but the final regulations may provide additional clarity on these issues.

^[1] Unless otherwise indicated, references to sections are to sections of the Internal Revenue Code of 1986, as amended.

^[2] On April 7, 2023, the IRS and the Treasury made an update to the Notice via online modification which provided for clarification on the beginning of construction date.

[3] Notice 2013-19 set out the initial “start of construction” rules for PTC projects (and PTC-eligible projects that elected to use the ITC), and Notice 2018-59 set out corresponding rules for solar projects under the ITC. Several other Notices were issued to further modify aspects of the start-of-construction rules, including the requirement that the taxpayer maintain a continuous program of construction or make continuous efforts to complete construction, in light of changes in the law, business changes, and the need for greater clarity on some points.

MEET THE TEAM



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