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REPORT



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Internal Revenue Service's Energy Community Bonus Guidance Provides Welcome Clarity

*By Amish Shah, Brad M. Seltzer, Nicole M. Elliott, Mary Kate Nicholson, Roger David Aksamit, Joshua L. Belcher, Joshua David Odintz, Kenneth W. Parsons, Daniel Graham Strickland, Rachel T. Provencher, Simon Levenson, Meaghan A. Colligan and Nicholas William Targ**

In this article, the authors review guidance released recently by the Internal Revenue Service regarding the energy community bonus credit available under various section of the Internal Revenue Code.

After much anticipation, the Internal Revenue Service (IRS) released guidance regarding the energy community bonus credit under Internal Revenue Code (Code) Sections 45, 48, 45Y and 48E, which also is applicable for purposes of Section 48C. The guidance issued by the IRS in Notice 2023-29:¹

- Addresses the timing of eligibility for an energy community determination;
- Clarifies the three broad categories of energy communities and provides resources to determine whether a project is located within certain energy communities; and
- Provides rules for projects only partially located in energy communities.

The energy community bonus, made available under the Inflation Reduction Act² generally increases the value of a credit by 10 percent (the bonus amount is reduced if the prevailing wage and apprenticeship requirements are not satisfied) for projects located in an energy community. Further, projects seeking an allocation under Section 48C may benefit from being in an energy community.

TIMING FOR DETERMINATION OF AN ENERGY COMMUNITY

For Sections 48 and 48E – the investment tax credit, and its successor, the technology neutral investment tax credit – a qualified facility generally must be located in an energy community as of the placed-in-service date to qualify for the bonus.

The Sections 45 and 45Y – the production tax credit, and its successor, the technology neutral production tax credit – are available for 10 years after a

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¹ <https://www.irs.gov/pub/irs-drop/n-23-29.pdf>.

² P.L. 117-169.

qualified facility is placed in service (PTC tax period). Under the guidance, a qualified facility must be located in an energy community, with the determination generally made yearly during the period in which the tax credit is available. Because the energy community determination is made on an annual basis for Sections 45 and 45Y, if a project is placed in service and initially does not qualify but later qualifies as an energy community due to changes in the energy communities such as changes to census tracts or unemployment rate changes, the project will qualify for the energy community bonus in such taxable year and any subsequent taxable year that meets the energy community requirements.

Notice 2023-29 provides a safe harbor giving taxpayers clarity earlier in the development of a project. Applicable for projects that begin construction on or after January 1, 2023, the safe harbor provides that if a taxpayer begins construction of a project in an energy community as of the beginning of construction (BOC) date, then, with respect to that project, the location will continue to be considered an energy community for the duration of the credit period for Sections 45 and 45Y or on the placed-in-service date for Sections 48 and 48E, even if the community ceases to qualify as an energy community during the PTC tax credit period or on the placed in service date.³

The limitation of the availability of the safe harbor to projects that begin construction on or after January 1, 2023, was added to Notice 2023-29 after initial publication of the guidance. It is unclear what the policy reasoning behind the limitation is, as it creates winners and losers solely based on the beginning construction date. Notably, taxpayers who began construction in 2022 to avoid application of the prevailing wage and apprenticeship requirements (including those who began construction after the publication of the prevailing wage and apprenticeship guidance in Notice 2022-61 on November 29, 2022) are precluded from using the safe harbor with respect to the energy community bonus requirement.

HOW TO DETERMINE IF A PROJECT IS LOCATED IN AN ENERGY COMMUNITY

Figure 1 summarizes the IRS guidance with respect to the three categories of energy communities in which a project must be located for entitlement to the energy community bonus.

³ The Notice references the Section 45 and Section 48 beginning of construction notices for purposes of determining when construction begins. Taxpayers will need to carefully determine when construction begins under guidance provided by the IRS.

Categories	Definition	Safe Harbors
Brownfield Category	<p>Defined in 42 U.S.C. § 9601(39)(A) as 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 certain mine-scarred land. A brownfield site does not include the categories of property described in 42 U.S.C. § 9601(39)(B), which are generally those already subject to certain federal or state cleanup actions under federal grants of authority.</p>	<p>Given the broad nature of the definition of a brownfield site, IRS has created three specific categories of projects that, if satisfying the terms of the Notice and relevant Amendments, will have certainty that they will be considered projects by the IRS. IRS refers to these as the “Safe Harbors.”</p> <ol style="list-style-type: none"> 1. Projects previously assessed as a brownfield site through a federal, state, territory or federally recognized Indian tribal brownfield program. The IRS indicates that potential sites may be identified on EPA’s Cleanups in My Community webpage,⁴ or on similar webpages maintained by states, territories or for federally recognized Indian tribes. Projects may also be able to use historic records indicating participation in a program obtained through due diligence. 2. Phase II environmental site assessment performed under the most recent ASTM standard (i.e. ASTM E1903 at the time of publication) that confirms the presence of a hazardous substance, pollutant or contaminant. 3. Projects with a nameplate capacity of not greater than 5 megawatts (MW) of alternating current (AC), if an ASTM E1527 Phase I Environmental Site Assessment (Phase I Assessment) has been completed, identifying the presence or potential presence of a hazardous substance, pollutant or contaminant.

⁴ <https://www.epa.gov/cleanups/cleanups-my-community>.

<p>Statistical Area Category</p>	<p>Metropolitan statistical area (MSA) or non-MSA, which</p> <ul style="list-style-type: none"> • Has (or, at any time during the period beginning after December 31, 2009, had) 0.17 percent or greater direct employment or 25 percent or greater local tax revenues related to the extraction, processing, transport or storage of coal, oil or natural gas, and • Had an unemployment rate at or above the national average unemployment rate for the previous year 	<p>Taxpayers can reference the Mapping Tool⁵ provided by the Interagency Working Group. The Mapping Tool shows the MSAs and non-MSAs that have had 0.17 percent or greater direct employment related to extraction, processing, transport or storage of coal, oil or natural gas. The IRS will update the map to show which of those areas also has an unemployment rate at or above the national average unemployment rate for the previous year once the rates for 2022 are released in 2023. After that information is included in the Mapping Tool, taxpayers will be able to use the map to identify many of the energy communities that qualify under this category. The guidance does not provide information regarding qualification under the areas with 25 percent or greater local tax revenues opportunity but instead requests comments on how that determination should be made.</p>
<p>Coal Closure Category</p>	<p>Census tract (or adjoining tract) where</p> <ul style="list-style-type: none"> • A coal mine has closed after 1999, or • A coal-fired electric generating unit was retired after 2009 <p>An adjoining tract is any tract that touches another tract at any single point.</p>	<p>Taxpayers can reference the Mapping Tool provided by the Interagency Working Group. The Mapping Tool shows the areas that qualify under this category.</p>

Figure 1

⁵ <https://energycommunities.gov/energy-community-tax-credit-bonus/>.

PROJECTS PARTIALLY LOCATED IN AN ENERGY COMMUNITY

A project is treated as located in or placed in service within an energy community, thus qualifying for the 10 percent bonus, if one of the following two tests is met.

Nameplate Capacity Test

Projects with nameplate capacity must use this test. A project that has nameplate capacity is considered located in, or placed in service in, an energy community if at least 50 percent of the project's nameplate capacity is in an area that qualifies as an energy community.

$$\text{Percentage} = \frac{\text{Nameplate capacity of electric generating units within the energy community}}{\text{total nameplate capacity of all electric generating units}}$$

For energy storage projects, the nameplate capacity for purposes of this rule means the usable energy capacity (in megawatt hours, or MWh). Useable energy capacity is the energy storage device capacity (in megawatts, or MW) multiplied by the duration hours of that storage capacity (h).

For offshore wind projects with no generation units in a census tract, MSA or non-MSA, the nameplate capacity for purposes of this test is determined by reference to the land-based power conditioning equipment that conditions energy generated by the offshore wind project for transmission, distribution or use and that is closest to the point of interconnection.

Footprint Test

A project is considered located in or placed in service within an energy community if at least 50 percent of its square footage is in an area that qualifies as an energy community.

$$\text{Percentage} = \frac{\text{Square footage located in an energy community}}{\text{total square footage of the project}}$$

Where there is a risk that the nameplate test or the footprint test (as applicable) will not be satisfied, a more detailed analysis may need to be undertaken to determine what property is included in the project. A careful determination of the property that is included in the project is important because of the 50 percent thresholds in the nameplate test and the footprint tests are cliffs, and projects that do not meet the applicable 50 percent threshold lose the ability to access the energy community 10 percent bonus.

SUMMARY

- The IRS released guidance regarding the energy community bonus credit under Code Sections 45, 48, 45Y and 48E.
- The energy community bonus, made available under the Inflation Reduction Act, generally increases the value of a credit by 10 percent (the bonus amount is reduced if the prevailing wage and apprenticeship requirements are not satisfied) for projects located in an energy community.
- Further, projects seeking an allocation under Section 48C may benefit from being in an energy community.

TAKEAWAYS AND NEXT STEPS

The issuance of this energy community bonus guidance generally has been well received.

For many projects for which construction began before January 29, 2023 (either under the project's initial construction schedule or to automatically satisfy the prevailing wage and apprenticeship requirement), careful consideration will need to be given as to whether the project was in an energy community at the time construction began.

For projects that have not yet begun construction, consideration will need to be given as to when to begin construction to ensure that the energy community bonus will be available.

Finally, as the U.S. Department of the Treasury and the IRS release further Inflation Reduction Act guidance, there may be additional considerations arising from the interplay between such guidance that will need to be navigated to maximize the amount and certainty of the tax credits available for a project.