# Inflation Reduction Act: Considerations for Tax-Exempt Entities

## How Tax-Exempt Entities Can Benefit from Tax Incentives in the Inflation Reduction Act

The Inflation Reduction Act (IRA), which was signed into law on August 16, 2022,[1] includes $386 billion of climate and energy spending and tax breaks, with varied incentives designed to reduce the cost of a transition to cleaner energy.[2] The investments in the IRA are designed to reduce greenhouse gas emissions by approximately 40% (compared to 2005) by 2030.[3]

IRA's tax incentives could provide state and local governments, transit agencies, public utilities, school districts, higher education institutions, housing agencies, and non-profits, the opportunity to fund a broad range of new (clean) energy projects. The tax incentives created by IRA could significantly shift how tax-exempt entities generate power and electricity.

| Examples of Projects with Potential to be Subsidized through IRA Tax Incentives: |
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| Installation of energy facilities (e.g., solar, wind, biogas projects, microgrid facilities) |
| Conversion of vehicle fleets to electric or hybrid (e.g., police cars, buses) |
| Electric vehicle deployment |
| Use of renewable fuels |
| Energy efficient building design and construction in new/and or existing buildings |

## Tax Incentives for Tax-Exempt Entities[4]

In the IRA, many of the tax incentives available to tax-exempt entities take the form of a one-time direct payment from the U.S. Treasury. This payment would be made on a reimbursement basis for qualified costs. In one case (i.e., the Production Tax Credit for renewable energy facilities), the incentive takes the form of a subsidy over time. There is also an exception for energy efficiency projects in commercial buildings; this tax incentive takes the form of a tax deduction that can potentially be traded to a tax-paying entity.

For certain incentives, the base incentive is increased by five times if the applicant abides by prevailing wage standards (i.e., Davis-Bacon wage requirements) and apprenticeship requirements. On November 30, 2022, the U.S. Treasury published initial prevailing guidance governing the fair wage and apprenticeship requirements. Some incentives also provide additional opportunities to increase the base credit (e.g., located in areas that are most impacted by a transition to clean energy) and/or decrease the base credit by using tax-exempt financing for the balance of the project costs.

## Summary of Select Tax Incentives

**Installation of renewable energy facilities.**[5] There are several provisions that apply to renewable energy projects, such as solar and wind facilities and biogas projects. The entity could elect to use either the:

- *Production Tax Credit (PTC).* Provides a subsidy of $26/MWh† of energy generated for the first 10 years of production. The PTC is adjusted for inflation.
- *Investment Tax Credit.* The IRS will provide a one-time, direct payment equal to 30% of the eligible construction costs of the facility.† This tax credit can also be used for qualified biogas property, such as biogas digestors used in wastewater facilities.

**Transportation Related Credits.**[1] There are several provisions that could subsidize the cost of the transition to a cleaner fleet, including the upfront vehicle purchases, the installation of Electric Vehicle (EV) charging stations, and the ongoing purchase of alternative fuels:

[1] Inflation Reduction Act, Pub. L. No. 117-169, 136 Stat. 1818 (2022); https://www.congress.gov/bill/117th-congress/house-bill/5376/text
[2] "What's in the Inflation Reduction Act?" Committee for a Responsible Federal Budget, last updated September 7, 2022, https://www.crfb.org/blogs/whats-inflation-reduction-act
[3] "New OMB Analysis: The Inflation Reduction Act Will Significantly Cut the Social Costs of Climate Change," The White House, August 23, 2022, https://www.whitehouse.gov/omb/briefing-room/2022/08/23/new-omb-analysis-the-inflation-reduction-act-will-significantly-cut-the-social-costs-of-climate-change/#:~:text=The%20new%20analysis%20finds%20that,to%20%241.9%20trillion%20by%202050.
[4] "Tax Provisions in the Inflation Reduction Act of 2022," Congressional Research Service, August 10, 2022, https://crsreports.congress.gov/product/pdf/R/R47202
[5] "The Renewable Electricity Production Tax Credit: In Brief (R43453)," Congressional Research Service, April 29, 2020, 2020. https://crsreports.congress.gov/product/pdf/R/R47202
† Assuming prevailing wage and apprentice requirements are met

- *Qualified Commercial Clean Vehicles.* Tax-exempt entities could receive a direct payment from the IRS for the purchase of any vehicle to be use on public roadways. The payment amount is subject to multiple tests based on vehicle weight, battery capacity, and fuel type. The maximum amount of the payment would be:
  - Vehicles <7 tons (e.g., police cars): $7,500/vehicle
  - Vehicles ≥ 7 tons (e.g., buses, garbage trucks): $40,000/vehicle
- *Alternative Fuel Refueling Property Credit.* Tax-exempt entities could receive a direct payment from the IRS for the installation of EV charging stations and the supporting infrastructure. The maximum payment would be 30% of the qualified costs[†] or $100,000 per EV charging station location. After December 31, 2022, this credit is only available if the EV charging station is built in a low-income or rural census tract.
- *Alternative Fuel Tax Credit*. Tax exempt entities could receive a direct payment for the use of biofuels or other alternative fuels. This incentive expires at the end of 2024.
  - $0.50 per gallon discount for alternative fuels
  - $1.00 per gallon discount for biodiesel and renewable diesel

**Energy Efficient Commercial Buildings Property Tax Deduction.**[6] This provision could reduce the cost of installing energy efficient property in new or existing systems, in at least one of three systems: 1) interior lighting systems, 2) heating, cooling, ventilation, & hot-water or, 3) the building's envelope. The incentive is based on a sliding scale ranging from $2.50 per square foot[†] to $5.00 per square foot. There is no direct payment option for this credit. Monetization of the credit could be achieved through transfer of the credit to the designer of the building or retrofit plan.

## Actions to Consider Now

Inflation Reduction Act implementation is ongoing- the U.S. Department of Treasury is regularly releasing guidance and updates.[7] There are many actions governments can consider taking to stand ready throughout the implementation period:

- Identify & evaluate potentially applicable IRA incentives. PFM can assist in comparing the election of the Production Tax Credit vs. the Investment Tax Credit and in considering the impact of tax-exempt debt on the subsidy.
- Consider accelerating or adding projects in light of the expiration of and/or changes to the incentives over time.

PFM can assist clients in developing and executing a strategy to harness federal incentives (e.g., tax incentives, grants) in the IRA and complementary programs in the Infrastructure Investment and Jobs Act. To learn more about how PFM can assist your locality to optimize federal funding, please reach out to your PFM representative or send an email to federalinfrastructure@pfm.com.

[6] "IRC 179D Energy Efficient Commercial Building Deduction," Internal Revenue Service, https://www.irs.gov/pub/irs-utl/irc-179d-energy-efficient.pdf

[7] "Treasury Announces Information Timeline for Inflation Reduction Act Tax Implementation," U.S. Department of the Treasury, December 19, 2022, https://home.treasury.gov/news/press-releases/jy1173

[†] Assuming prevailing wage and apprentice requirements are met