BRACEWELL

INSIGHTS

Treasury Department and IRS Release Guidance on the Advanced Energy Project Credit Allocation Program Under Internal Revenue Code Section 48C(e)

February 27, 2023

*By: **Steven J. Lorch** and **Elizabeth L. McGinley***

On February 13, 2023, the Treasury Department and the Internal Revenue Service (the IRS) released ***Notice 2023-18*** (the Notice), which established the program (the Allocation Program) to allocate $10 billion of advanced energy project credits (AEPCs) pursuant to section 48C(e),[1] which was enacted as part of the Inflation Reduction Act of 2022 (the IRA).[2] The goal of the program is to expand U.S. manufacturing capacity and quality jobs for clean energy technologies (including production and recycling), to reduce greenhouse gas emissions in the U.S. industrial sector, and to secure domestic supply chains for critical materials that serve as inputs for clean energy technology production.

Key Takeaways

- The Treasury Department and the IRS anticipate providing at least two rounds of AEPC allocations.
- The Notice provides an initial framework and timeline for the first allocation round (Round 1).
- Pursuant to Round 1, the IRS anticipates allocating $4 billion of AEPCs of which approximately $1.6 billion will be allocated to projects located in Energy Communities (defined below).
- The Treasury Department and the IRS intend to issue supplemental guidance with respect to Round 1 on or before May 31, 2023 (the Additional Guidance).

- Taxpayers may submit initial concept papers (Concept Papers) for Round 1 projects until July 31, 2023.

- Taxpayers that timely submit a Concept Paper for a project may submit a full Round 1 application (the AEPC Application). The deadline for APEC Applications will be provided in the Additional Guidance.

- The IRS will consider making an AEPC allocation for a project only if the Department of Energy (DOE) provides to the IRS a recommendation and ranking for the project. The DOE will provide a recommendation and ranking for a project only if DOE determines that the project has a reasonable expectation of commercial viability and merits a recommendation based on criteria to be provided in the Additional Guidance.

- The Notice confirms that a taxpayer is not eligible for the AEPC for any investment for which a credit is allowed under section 48 (energy credit), section 48A (qualifying advanced coal project credit), section 48B (qualifying gasification project credit), section 48E (clean electricity investment credit), section 45Q (credit for carbon oxide sequestration), or section 45V (credit for production of clean hydrogen) (collectively, the Specified Credits).

The AEPC under the IRA

Section 48C was enacted by the American Recovery and Reinvestment Act of 2009 (Previous Section 48C) and created a federal income tax credit for certain investments (Qualified Investments) in depreciable property necessary for the operation of qualifying advanced energy projects (Qualifying Projects).

The total credit allocation under Previous Section 48C was capped at $2.3 billion. The IRA provided an additional allocation of $10 billion, not less than $4 billion of which must be allocated to projects located in census tracts (or adjoining tracts) in which a coal mine has closed since 2000 or a coal-fired plant has been retired since 2010 (an Energy Community).

The IRA expanded the scope of projects that are eligible for the AEPC beyond the projects that were eligible for credits under Previous Section 48C. Qualifying Projects now include:

- Projects that re-equip, expand, or establish an industrial or manufacturing facility for the production or recycling of certain property types, including (1) equipment that produces energy from the sun, water, wind, geothermal deposits, or other renewable resources, (2) fuel cells, microturbines, or energy storage equipment, (3) electric grid modernization equipment, (4) equipment for the capture, removal, usage, or sequestration of carbon oxide emissions, and (5) equipment that refines, electrolyzes, or blends any fuel, chemical, or product which is renewable or low-carbon and low-emission.

- Projects that re-equip any industrial or manufacturing facility with equipment designed to reduce greenhouse gas emissions by at least 20 percent through the installation of (1) low- or zero-carbon process heat systems, (2) carbon capture, transport, utilization, and storage systems, (3) systems improving energy efficiency and reducing waste from industrial processes, or (4) any other industrial technology designed to reduce greenhouse gas emissions, as determined by the Secretary of the Treasury.

- Projects that re-equip, expand, or establish an industrial facility for the processing, refining, or recycling of critical materials (generally, materials and minerals used in the production of batteries).

Under the IRA, the AEPC is equal to 30 percent of a taxpayer's Qualified Investment in any Qualifying Project, provided that the project satisfies the prevailing wage requirements and the apprenticeship requirements. The APEC is not eligible for the domestic content bonus, the energy communities bonus, or any other bonus credit under the IRA.

General Procedure for Round 1

The Notice provides a general procedure for Round 1, as follows:

- **Taxpayer submits a Concept Paper to DOE**. A taxpayer that intends to apply for an AEPC allocation must submit a Concept Paper for the project prior to July 31, 2023. The Notice provides limited guidance regarding the criteria on which Concept Papers will be evaluated, with the promise of further detail in the Additional Guidance.[3]

- **DOE reviews Concept Paper**. DOE will review the taxpayer's Concept Paper and send the taxpayer a letter encouraging or discouraging the submission of an AEPC Application. The taxpayer may submit an AEPC Application regardless of whether DOE encourages or discourages submission. If, however, DOE's letter discourages submission, the project, as proposed, would be unlikely to receive a DOE recommendation based on the information provided in the Concept Paper.

- **Taxpayer submits an AEPC Application and DOE performs initial review**. The taxpayer will submit the AEPC Application and DOE will review for compliance with eligibility and other threshold requirements, including, for example, whether the project satisfies the definitional requirements of a qualified advanced energy project.

- **DOE conducts a full review of the AEPC Application**. If the AEPC Application satisfies the eligibility and other threshold requirements described above, DOE will perform a full technical review of the AEPC Application. DOE will provide a recommendation and ranking only if it determines that the project has a reasonable expectation of commercial viability and merits a recommendation based on criteria to be provided in the Additional Guidance. The Notice does not offer a full description of DOE's technical review process, although it suggests that the following factors will be relevant: (1) the project's impact on domestic job creation, (2) the project's impact in avoiding or reducing air pollutants or emissions of greenhouse gases, (3) the project's community benefits, which may include community and labor engagement and commitment to high quality and accessible jobs and workforce pathways, (4) whether the project will address specific gaps, vulnerabilities, or risks in the domestic production of clean energy products, and (5) whether the taxpayer may have a connection with a foreign country of risk (including China, Russia, Iran, and North Korea based on recent DOE guidance) that could frustrate the policy goals of the Allocation Program. In addition, to strengthen U.S. industrial competitiveness and clean energy supply chains, DOE may give priority to projects not otherwise eligible for federal support from DOE or under the IRA.

- **DOE provides the IRS with a recommendation and ranking for the project**. DOE will provide a recommendation to the IRS regarding the acceptance or rejection of each AEPC Application and a ranking of the applications. DOE also will determine which projects are eligible for an allocation of the $1.6 billion of AEPCs that are reserved for projects located in Energy Communities.[4] If DOE does not provide a recommendation for a project, the IRS will not consider the project's AEPC Application.

- **IRS makes a decision with respect to the project**. The IRS will send a letter to the taxpayer allocating AEPCs to the project or denying the requested allocation. The amount of allocated APECs will be based on the dollar amount of the taxpayer's Qualified Investment in the Qualifying Project and whether the taxpayer intends to satisfy the prevailing wage requirements and apprenticeship requirements with respect to the project. A taxpayer that receives a denial of AEPCs may be eligible to request a debriefing during which DOE will present the strengths and weaknesses of the rejected AEPC Application to enable the taxpayer to improve the application in future allocation rounds.

A taxpayer must notify DOE that the project has met certain certification requirements within two years of receiving an AEPC allocation.[5] The IRS, after receiving notification from DOE that the taxpayer has met these requirements, will certify the project by sending a certification letter to the taxpayer. Within two years of receiving this letter, the taxpayer must notify DOE that the project has been placed in service. The taxpayer may claim the AEPCs on its income tax return for the taxable year in which the project was placed in service. If the taxpayer has not placed the project in service within the required two-year period or has not notified DOE that the project has been placed in service within this period, the AEPCs allocated to the taxpayer's project will be forfeited.

Anti-Stacking Rules

The Notice confirms that a taxpayer is not eligible for AEPCs for any investment for which a Specified Credit is allowed. The taxpayer, both on its AEPC Application and at the time it notifies DOE that a project has been placed in service, must certify under penalties of perjury that the taxpayer has not claimed a Specified Credit for the relevant investment. If the IRS determines that any Specified Credit has been claimed for an investment, the IRS will not allocate AEPCs to the investment and any previous AEPC allocation for the investment will become void.

The Notice also confirms that property will not be treated as an eligible component for purposes of section 45X (advanced manufacturing production credit) if any portion of the facility that produced the property is taken into account for purposes of section 48C after the date of the IRA's enactment (August 16, 2022). Guidance regarding this limitation will be provided in additional guidance under Section 45X.

Additional Aspects of the Notice

The Notice also provides:

- Further definitional guidance regarding various types of Qualifying Projects;
- A procedure under which a project transferee can apply to receive the benefit of a transferor's AEPC allocation;
- Guidelines regarding a change in facts from those set forth in a Concept Paper or AEPC Application that can result in the voiding of an AEPC Application or a forfeiture of AEPCs for a project;
- The reallocation of AEPCs for which an IRS certification has been revoked; and
- Special rules for taxpayers that self-construct projects to claim AEPCs in an earlier taxable year with respect to qualified progress expenditures.

Looking Ahead

The Notice contains practical and constructive guidance for taxpayers considering an AEPC Application. The Notice, however, does not provide a complete description of the information that will be required in Concept Papers and AEPC Applications, or the criteria by which projects will be evaluated.

1. All section references in this article are intended to refer to the Internal Revenue Code of 1986, as amended.

2. Follow ***this link*** for a general summary of the IRA and follow ***this link*** for our coverage of recent guidance regarding the prevailing wage requirements and the apprenticeship requirements under the IRA.

3. The Notice provides that the criteria may include "eligibility requirements, definitions for qualifying advanced energy projects, reasonable expectation of commercial viability, and other factors described in the [Additional Guidance]."

4. The Notice provides that the Additional Guidance will reference a mapping tool that will enable taxpayers to determine whether a project is located in an Energy Community.

5. A project is eligible for certification only if the taxpayer has received all permits from federal, state, tribal, and local governmental bodies for construction of the project at the planned location, including environmental authorization or reviews necessary to commence construction of the project.