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Tax Update January 14, 2025

IRS and Treasury Issue Final Regulations for Tech-Neutral Tax Credits for Clean Energy Projects

This update discusses recently issued final regulations under sections 45Y and 48E regarding tax credits enacted as part of the Inflation Reduction Act of 2022 for clean energy projects.[1]

On January 7, 2025, the IRS and Treasury released final regulations relating to tech-neutral tax credits for clean energy projects that were enacted as part of the Inflation Reduction Act (the "Final Regulations") and that are scheduled to be published in the Federal Register on January 15, 2025. Please see the unpublished version of the Final Regulations here. The Final Regulation are largely consistent with proposed regulations published in May 2024 (the "Proposed Regulations") (please see our earlier alert here), but do include a few notable adjustments.

Background on Sections 45Y and 48E

Beginning in 2025, sections 45Y and 48E (respectively, the tech-neutral production tax credit (PTC) and tech-neutral investment tax credit (ITC)) replace many of the credits in sections 45 (the legacy PTC) and 48 (the legacy ITC).[2] In lieu of prescribing a list of credit-eligible technologies, as sections 45 and 48 do, sections 45Y and 48E contemplate a "technology neutral" system, where energy generation or storage technology qualifies for credits by satisfying a "zero or negative" greenhouse gas (GHG) emissions standard. These credits are designed to "encourage innovation by allowing new zero-emissions technologies to develop over time" by providing "durable incentives" for making investments in clean energy technology.[3]

Qualifying Technologies

The Proposed Regulations included a list of technologies that are treated as having a GHG emissions rate that is not greater than zero (the Per Se List), including wind, solar, geothermal, marine and hydrokinetic, and nuclear energy (both fission and fusion) projects. Although taxpayers requested that additional technologies be added to the Per Se List, the Final Regulations include no new technologies. In addition, the IRS is required to publish an annual table that includes the GHG emissions rates for a variety of types of technology. Some taxpayers had worried that the technologies on the Per Se List would be credit eligible only if they were included in the annual table, but the IRS resolved this issue in the Final Regulations by explicitly deeming technologies on the Per Se List to be included on the annual table with a GHG emissions rate of zero or less.

With respect to technologies *not* included on the Per Se List, some taxpayers had requested that the first annual table be released at the same time as the Final Regulations, but this request was not granted. In the preamble to the Final Regulations, the IRS and Treasury noted that in light of the time and effort needed to conduct the relevant emissions analysis, the IRS could "not commit to a specific timeline for publication" of the initial annual table.

LCAs and C&G Tech

As described in our alert on the Proposed Regulations, GHG emissions rates for combustion and gasification facilities (C&G Facilities) must be determined pursuant to a complicated lifecycle analysis (LCA) model that considers emissions beginning with feedstock generation or extraction and ending with the end of the electricity production process. For technologies not addressed in the annual table, taxpayers will likely need to pursue a provisional emissions rate from the IRS, which will require first receiving an emissions value from the Department of Energy in a process determined based on an LCA model designated by the IRS. The Final Regulations include numerous additional details regarding various aspects of how LCA determinations will be made, including details related to accounting for "alternative fates" and avoided emissions (*i.e.*, estimated emissions associated with the feedstock's production and use or disposal if the feedstock had not been diverted to the production of electricity), and details related to the required time horizon and spatial scope (which could, depending on the circumstances, require an examination of local, regional, domestic, or international markets and supply chains).

80/20 Rule Clarity

The Proposed Regulations provided guidance on the tax credit implications of retrofitting facilities after they had already been placed in service, drawing a distinction between capacity increases and capital expenditures that do not increase capacity. Capital expenditures that do not increase capacity yield tax credits (either a new, tech-neutral ITC under section 48E or a new period of tech-neutral PTCs under section 45Y) only where they are substantial enough to satisfy the 80/20 rule (see our discussion of this rule here), such that the facility will be treated as newly placed in service. Facilities for which certain other credits (including the legacy PTC and ITC) have been claimed, however, are ineligible for tech-neutral credits. Although the Final Regulations generally retain each of these rules[4], one question that had not been explicitly answered by the Proposed Regulations was whether, assuming the 80/20 rule is satisfied, it would be feasible to claim tech-neutral credits on a retrofitted facility in a circumstance where legacy PTCs or ITCs (under section 45 or 48) had been claimed for the predecessor facility. The Final Regulations make clear that the answer is yes.

Qualified Facilities and Prevailing Wage and Apprenticeship Rules

Credit eligibility is determined on a "qualified facility"-by-"qualified facility" basis, and this concept plays an important role throughout the tech-neutral guidance. The Final Regulations generally retain the definition of "qualified facility" from the Proposed Regulations,[5] but also make clear that the prevailing wage and apprenticeship rules[6] apply on a "qualified facility"-by-"qualified facility" basis, contrary to the existing section 48 ITC rules, which apply these rules on an "energy project"-by-"energy project" basis. As a result of this difference (which also applies for purposes of various credit adders), the prevailing wage and apprenticeship requirements (and the bonus credit requirements) that apply under 48E are more stringent than those that apply under 48.

Other Items

- As described in our alert on the Proposed Regulations, the Inflation Reduction Act included an unfortunate bar on claiming a tech-neutral ITC for a "building or its structural components." Although the Final Regulations of course do not eliminate this statutory restriction, the preamble does include some discussion that should be helpful to operators of certain nuclear facilities. In particular, the preamble to the Final Regulations confirms that nuclear containment structures are not considered to be buildings because they are essentially items of specialized equipment, qualifying under the rule that a structure is not considered a building if it is essentially an item of machinery or equipment.

- Under the Proposed Regulations, hydrogen energy storage property was required to store hydrogen solely used as energy (and not for other purposes, such as fertilizer). The IRS received numerous comments criticizing this non-statutory requirement, which was referred to as the "End Use Requirement." After consideration of the comments, the IRS agreed to abandon the End Use Requirement in the Final Regulations, meaning that hydrogen storage property will be able to store hydrogen for other purposes, such as the production of fertilizer.[7]

- As described in our alert on the Proposed Regulations, a taxpayer must own at least a fractional interest in an entire unit of qualified facility to be eligible to claim the tech-neutral ITC. The Final Regulations maintain this requirement but clarify that the rule does not require a taxpayer claiming the tech-neutral ITC to own all "integral property"[8] and include an example that should be helpful to taxpayers who own certain hydropower facilities, clarifying that these taxpayers can claim the tech-neutral ITC, even if the associated dam is owned by a governmental entity.

- The IRS and Treasury noted in the preamble to the Final Regulations that Notice 2008-60 would not apply to section 45Y because section 45Y provides for equipping a qualified facility with a metering device. Accordingly, if a taxpayer does not equip a facility with a metering device and claims the section 45Y credit, then that taxpayer should be particularly cautious in ensuring that the initial sale of electricity is not to a related person (because the taxpayer would not be permitted to rely on the former guidance under section 45 that an initial sale to a related person is permitted if the ultimate end user is unrelated).

Congressional Review Act

Because the Final Regulations will be published in the Federal Register on January 15, 2025, the incoming 119th Congress and President Trump will be able to overturn the Final Regulations under the special Congressional Review Act procedures. Under the Congressional Review Act, a final agency rule can be overturned under a special expedited procedure requiring a joint resolution of disapproval by both houses of Congress (in a process requiring very little Senate floor time) and signature by the President.[9] If Congress enacts such a joint resolution overturning a regulation, the agency may not reissue the rule "in substantially the same form" unless Congress passes legislation authorizing such a rule.[10]

[1] Unless indicated otherwise, all "section" references are to the Internal Revenue Code of 1986, as amended (the "Code"), and all "Treas. Reg. §" are to the Treasury regulations promulgated under the Code, in each case as in effect as of the date of this alert. The actual name of Public Law No. 117-169, commonly referred to as the Inflation Reduction Act of 2022, is "An Act to provide for reconciliation pursuant to title II of S. Con. Res. 14."

[2] Most of the credits under sections 45 and 48 generally will not be available to projects the construction of which begins after December 31, 2024.

[3] Treas. Dept., *U.S. Department of the Treasury Releases Final Rules for Technology-Neutral Clean Electricity Credits*, available here.

[4] The Final Regulations do include some incremental detail regarding *how* to determine whether there has been a capacity increase. Under these rules, if available, a taxpayer must utilize a modified or amended facility operating license from the Federal Energy Regulatory Commission or Nuclear Regulatory Commission (or related reports). Otherwise, taxpayers are to use nameplate capacity certified consistent with accepted industry standards, or a measurement standard published in the Internal Revenue Bulletin.

[5] A qualified facility includes a "unit of qualified facility," along with property owned by a taxpayer that is an integral part of the qualified facility (the integral part need not be a "qualified facility" in its own right). A "unit of qualified facility" is defined as all "functionally interdependent" components of property owned by a taxpayer that are operated together and can operate apart from other property to produce electricity. Components of property are "functionally independent" if the placement in service of each of the components is dependent on the placement in service of each other component to produce electricity. An "integral part" of a qualified facility is property used directly in the intended function of the facility that is essential to the completeness of its function.

[6] Please see our earlier client alert on the prevailing wage and apprenticeship rules, available here. An uncured failure to comply with the prevailing wage and apprenticeship requirements generally results in an 80% haircut to the otherwise available credit.

[7] In finalizing the section 48 regulations in December 204, the IRS and Treasury removed a similar end use requirement. For our alert related to the final regulations, please see here.

[8] Under the final section 48 regulations, it is also clear that a taxpayer need not own all "integral property."

[9] 5 U.S.C. § 802. In President Trump's first term, the Congressional Review Act was used to overturn 16 rules that had been enacted toward the end of the Obama administration. Congressional Research Service, The Congressional Review Act (CRA): A Brief Overview, available here. For more information on the Congressional Review Act, please see here.

[10] 5 U.S.C. § 801(b).

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Gibson Dunn lawyers are available to assist in addressing any questions you may have about these developments. To learn more about these issues, please contact the Gibson Dunn lawyer with whom you usually work, any member of the firm's Tax, Cleantech, Oil and Gas, or Power and Renewables practice groups, or the following authors:

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