For Public Utilities, the Road to Decarbonization Has Just Gotten Much Less Costly

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The Inflation Reduction Act of 2022 (IRA) has justifiably been referred to as the single largest and most important piece of energy and climate legislation enacted by the United States in the nation's history. The $370 billion that the federal government will spend directly and through tax incentives will inexorably move the country toward a clean energy revolution, substantially reducing greenhouse gas emissions, to the benefit of a vast array of industries, businesses, homeowners, and consumers.

Significantly, the IRA also provides enormous benefits that will help public utilities meet their own renewable energy goals, perhaps as soon as by the end of this decade. As discussed below, the IRA does that primarily through two methods: "direct pay" and "transferability."

Direct Pay

Federal law has long provided two clean energy tax credits: the investment tax credit (ITC) and the production tax credit (PTC). The ITC is a tax credit against the costs incurred in connection with investments in specified clean-power products; the PTC is a tax credit against the costs incurred in producing clean energy.

The IRA sets the base rates for both the ITC and PTC. Importantly, the IRA also provides that both may be increased in an amount up to five times the base rates where certain wage, domestic content, and location standards are met.

Neither tax credit, however, has been directly available to public utilities that did not have to pay federal income tax. Until now.

Under the IRA's direct pay provisions, public utilities are able to receive these credits on a per facility, per project, or per equipment basis directly from the federal government, in cash. There is no need to have a federal tax debt to offset against the credits.

The tax credits available for the direct pay provisions of the IRA range from a renewable electricity production tax credit, a carbon capture and sequestration tax credit, and a zero-emission nuclear power production tax credit, to a clean hydrogen tax credit, a clean electricity production tax credit, and a clean fuel production tax credit, among others.

Transferability

The IRA also provides for the transferability of the ITC and PTC. Put simply, public utilities can elect to have these tax credits transferred to unrelated third parties directly, without the need to engage in complicated tax financings. The transfers must be for cash, and the payments received are not taxable to the utilities.

Other Key Provisions

The IRA extends the ITC and PTC for 10 years – providing a good window during which public utilities may move to clean energy. The IRA also contains other tax credits that can benefit public utilities, such as a tax credit for electricity produced in a qualified nuclear power facility, as well as other incentives that public utilities may benefit from, such as $250 billion in loans that utilities can tap into to use to exit out of coal into clean energy.

With public utilities generating such a large percentage of American power, these IRA provisions take on even greater practical importance. Public utilities are now likely to plan new projects at a faster rate than before the IRA became law – and in fact may face increased pressure from state authorities to move more quickly to clean energy as state legislators and regulators begin to understand all of the benefits afforded to public utilities under the IRA and, correspondingly, to their customers from lower costs and cleaner air.

Clean power is coming, and sooner than many imagined possible just a few weeks ago. This article is informational only. You should consult an attorney before acting or failing to act. The law may change rapidly and no warranty is given. LOWNDES DISCLAIMS ALL IMPLIED WARRANTIES AND WITHOUT LIMITATION, ANY WARRANTY OF FITNESS FOR A PARTICULAR PURPOSE. ALL ARTICLES ARE PROVIDED AS IS AND WITH ALL FAULTS. Consult a Lowndes attorney if you wish to establish an attorney/client relationship.