

Summary of Treasury Proposed Rules on Monetization of Energy Tax Credits

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The U.S. Department of Treasury released two proposed rules clarifying new methods that tax-exempt entities and businesses with limited tax liability can use to monetize tax credits. The “Direct Pay” and “Transferability” methods of tax monetization were created by the Inflation Reduction Act and would ultimately allow for eligible businesses to incorporate a broader range of financing options for their clean energy projects.

The first method, [Direct Pay](#), known officially as elective payment of applicable credits, would be applicable to school districts, public utility districts, state universities, and government instrumentalities in U.S. territories who may receive cash payments for tax credits on qualifying investments. Direct Pay applies to 11 of 19 clean energy tax credits delineated in the Inflation Reduction Act, and only businesses that claim credit for three clean energy technologies can use direct pay – carbon capture, clean hydrogen, and advance manufacturing. Importantly, under Direct Pay, grant and forgivable loans would not reduce the benefit of the tax credits if they do not exceed the cost of the investment.

The second method, [Transferability](#), would allow businesses who have limited tax liability to transfer or sell their credits to other businesses by way of contract. The Treasury clarified that when using Transferability, which tax-exempt entities cannot use to sell or transfer unused credits, the risk that the credits would be recaptured falls on the buyer of the credits, not the seller. Transferability applies to 12 of 19 clean energy tax credits.

Separately, the Treasury published a [temporary rule](#) that establishes an online pre-filing process for entities seeking to use Direct Pay or Transferability. Entities are required to register their investments with the IRS on an online portal, which creates a registration number to be used on their tax forms. More information regarding this process is expected in the next months.

The IRS is soliciting public feedback on the rules until August 14, 2023, and will hold public hearings on the Direct Pay on August 21, 2023 and on the Transferability on August 23, 2023. Please let us know if you would like any assistance regarding these proposed rules or preparing comments.

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