

House Ways and Means Approves Green Energy Bill

SPEAKERS

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On September 15, the House Ways and Means Committee (Committee) approved a portion of bills drafted for inclusion in the \$3.5 trillion budget reconciliation legislation — the Build Back Better Act — including Subtitle G, Green Energy (Bill). The Bill contains significant changes to the production tax credit (PTC) and the investment tax credit (ITC), including 10-year extensions, a new two-tiered credit rate, new prevailing wage and apprenticeship requirements, increased credit amounts for projects satisfying domestic content requirements, a direct pay election, and an enhanced ITC for solar projects benefitting low-income communities. The Bill expands the PTC and ITC to cover a variety of other green energy technologies, including energy storage technology, and it includes a new ITC for transmission property. Although the approved text has yet to be released, we understand that the energy provisions in Subtitle G were approved in substantially the same form introduced [here](#) and as described in this [report by the Joint Committee on Taxation](#).

PTC and ITC Extensions

The modifications to the PTC and ITC would apply to projects placed in service after December 31, 2021. Accordingly, projects placed in service in 2021 would continue to qualify for PTCs and ITCs available under current law (e.g., the 60% PTC for wind projects that begin construction in 2020 or 2021, and the 26% ITC for solar projects that begin construction in 2020 or 2021).

The Bill would extend the PTC and ITC for wind and solar projects that begin construction prior to 2034, revive the PTC for solar projects, and expand the ITC to cover standalone energy storage projects.

The PTC rate for wind and solar projects would be 100% of the inflation-adjusted credit amount (currently 2.5 cents per kWh) (PTC Bonus Rate) if the prevailing wage and apprenticeship requirements discussed below are satisfied, construction on the project begins before the Bill's enactment date, or the applicable project has a maximum net output of less than 1 MW. Accordingly, the PTC Bonus Rate would restore the PTC to pre-phasedown levels. The PTC Bonus Rate would phase down to 80% of the credit amount for projects that begin construction in 2032 and to 60% for projects that begin construction in 2033, with no credit available for projects beginning construction thereafter.

The ITC rate for wind and solar projects would be 30% of the basis of qualified energy property (ITC Bonus Rate) if the prevailing wage and apprenticeship requirements discussed below are satisfied, construction on the project begins before the Bill's enactment date, or the applicable project has a maximum net output of less than 1 MW. Accordingly, the ITC Bonus Rate would restore the ITC to pre-phasedown levels. The ITC Bonus Rate would phase down to 26% for projects that begin construction in 2032 and to 22% for projects that begin construction in

2033, with no credit available for projects beginning construction thereafter.

Projects that do not satisfy the prevailing wage and apprenticeship requirements or other conditions described above would be eligible for a base rate equal to 20% of the applicable PTC Bonus Rate or ITC Bonus Rate (taking into account phasedowns).

- Two key consequences and potential planning opportunities flow from the Bill's transition rules and credit rates as currently drafted. First, projects that have begun construction before the date of enactment will not be subject to the prevailing wage and apprenticeship requirements. Second, credit rates for certain projects may be higher if they are placed in service in 2022 than they would be if they were placed in service in 2021.

Standalone Storage

The Bill would expand the ITC to cover standalone energy storage projects, including equipment that uses batteries, compressed air, pumped hydropower, and certain other storage property used to store energy for conversion to electricity (or, in the case of hydrogen storage, to store energy) with a capacity of at least 5 kWh.

- Under current law, energy storage property can qualify for the ITC only if it is part of an otherwise ITC-eligible project (typically solar or wind) and certain other requirements are met. An ITC for standalone energy projects would be a huge benefit for the development of these projects.

Prevailing Wage and Apprenticeship Requirements

The prevailing wage and apprenticeship requirements for the ITC and PTC are substantially similar. The prevailing wage provisions require that taxpayers ensure that any laborers and mechanics employed by contractors and subcontractors are paid prevailing wages during the construction of the applicable project and, in some cases, for the alteration and repair of such project for a defined period after the project is placed in service. The apprenticeship provisions require that no fewer than the applicable percentage of total labor hours of construction, alteration, or repair work prior to the project being placed in service are performed by qualified apprentices. The applicable percentage is 5% for projects that begin construction in 2022, 10% for projects that begin construction in 2023, and 15% thereafter. In addition, each contractor and subcontractor that employs four or more individuals to perform construction on a project must employ at least one qualified apprentice to perform such work. The Bill would provide taxpayers with the ability to cure the failure to satisfy the prevailing wage and apprenticeship requirements through payments to each worker paid below prevailing wage and penalty payments to the Treasury.

- Compliance with the prevailing wage and apprenticeship requirements will require planning and cooperation with EPC contractors and O&M providers to ensure the requirements are satisfied, compliance is verified, and there is adequate credit support. This is especially important for sponsors obtaining third-party financing.

Domestic Content Requirements

The Bill provides for an increased credit rate for projects that satisfy domestic content requirements, including that any steel, iron, or manufactured products used in the construction of the applicable project was produced in the U.S. Under the Bill, a manufactured product will be deemed to be U.S.-manufactured if not less than 55% of the total cost of the components of such product is attributable to components that are mined, produced, or manufactured in the U.S. The Treasury Secretary can provide exceptions to the domestic content requirements in certain circumstances (e.g., if the requirement results in cost increases of more than 25% or comparable products are not readily available in the U.S.). The increased credit rate is 10% of the inflation-adjusted credit amount for the PTC Bonus Rate and is 10% of the energy property basis (or 33% of the credit) for the ITC Bonus Rate.

- Note that the increase in the credit rate for the ITC (33%) is larger in absolute terms than the increase for the PTC (10%). It is unclear whether this was intentional or a drafting error. It is an open question as to how difficult it will be to satisfy this requirement.

Direct Pay Election

The Bill provides a direct pay election in lieu of a nonrefundable credit. The election applies to several credits (including the ITC, PTC, Section 45Q credit, and the ITC for transmission property) and can be made by tax-exempt entities and tribal entities in addition to typical taxpayers. Under the Bill, those who make the election are treated as having made a tax payment in the amount of the credit.

For the ITC, the PTC, and the transmission property ITC, the direct payment amount is determined by multiplying the credit by an applicable percentage. The applicable percentage is 100% if the project satisfies the domestic content requirement (or the requirement is deemed satisfied) or has a maximum net output of less than 1 MW. For all other projects, the applicable percentage is 100% if construction begins before 2024, 90% if the construction begins in 2024, 85% if construction begins in 2025, and 0% if construction begins thereafter.

- Direct pay would give sponsors a choice as to whether to pursue traditional tax equity financing or to “go it alone,” perhaps with traditional debt financing. There are pros and cons to a direct pay election even when there is no haircut. Going it alone might simplify the ownership structure and reduce the overall cost of financing (setting aside the tax benefits). However, the direct pay election does not monetize the depreciation, and it could be more difficult to achieve a full basis step-up (and therefore unlock the full credit value) in an ITC deal. Accordingly, we would expect to see a variety of different sponsor approaches to direct pay.
- The expansion of the entities eligible to elect direct pay means that pension funds, college endowments, tribes, states and municipalities, and investment funds with tax-exempt investors can now make investments in energy projects on a more equal footing.
- Because the phasedown does not start until 2024 and keys off a “beginning of construction” standard, we would expect to see significant numbers of projects eligible for direct pay well into the late 2020s.

Transmission Property ITC

The Bill would create a new ITC for electric transmission property. The ITC rates and phasedowns for transmission property would be the same as the ITC rates discussed above (e.g., 30% bonus rate, 6% base rate, and increases for domestic content).

Qualifying electric transmission property includes an electric transmission line that transmits at a voltage of at least 275 kV and has a transmission capacity of not less than 500 MW, as well as certain related transmission property if owned by the same taxpayer that owns the transmission line. Upgrades of an existing line are treated as replacements. In that case, the 500 MW capacity requirement is increased by the transmission capacity of the existing line, and the basis attributable to the existing line is not eligible for the credit.

- Given the nature of transmission property, we would expect the projects to be owned and the credits to be claimed by regulated utilities subject to normalization. We note that the Bill does not provide an exception from normalization.

Low-Income Community Requirements

The Bill would provide an enhanced ITC for solar projects with a nameplate capacity of 5 MW or less and located in a low-income community for which the Secretary makes an allocation of environmental justice solar capacity limitation. The annual capacity limitation is 1.8 GW for each calendar year 2022 through 2031, with rollover of unused allocations from the preceding year until 2033.

An additional 10% ITC is available for projects located in a low-income community (as defined for new markets tax credit purposes), and an additional 20% ITC is available for projects that are part of a “qualifying low-income residential building project” or a “low-income economic benefit project.” A solar project may qualify as part of a low-income residential building project if installed on a residential building that participates in one of several programs listed in the Bill and as part of a low-income economic benefit project if at least 50% of the financial benefits of the electricity produced are provided to households with income of less than 200% of the poverty line or at or below 80% of area median income.

While the Bill’s proposals favor the renewable energy industry as a whole, it will affect different industry participants differently. Furthermore, even the extensions, potential increases in the credits rates, and direct pay election come with significant new requirements. As a result, it is important for each industry participant to evaluate the Bill’s impact based on its own facts and circumstances.

We also note that the legislation is nowhere near final, and we expect to see many twists and turns along the way. Accordingly, it’s important to factor in the possibility of significant changes and to revisit the state of play regularly over the next few months. We will continue to provide updates. In the meantime, please feel free to contact us with any questions.

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