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Treasury and IRS Release Guidance on Energy Community Enhancements under the Inflation Reduction Act

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On April 4, the Treasury Department (Treasury) and the Internal Revenue Service (IRS) issued Notice 2023-29, which describes certain rules that Treasury and the IRS intend to include in forthcoming proposed regulations concerning energy communities. Under the Inflation Reduction Act of 2022 (IRA), projects located in an energy community qualify for enhanced credit amounts for several clean energy tax credits, including investment tax credits under Sections 48 and 48E (ITC) and production tax credits under Sections 45 and 45Y (PTC).

The regulations will apply to taxable years ending after April 4, 2023. Until the issuance of the proposed regulations, taxpayers may rely on the rules in Notice 2023-29.

Notice 2023-29 provides rules for determining what constitutes an energy community (the Brownfield Category, Statistical Area Category, and the Coal Closure Category described below) and for determining whether property is located in an energy community.

Brownfield Category

Brownfield sites are defined in the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) as real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant and certain mine-scarred land (each as defined in CERCLA). A brownfield site does not include the categories of property excluded from brownfield sites by CERCLA in 42 U.S.C. § 9601(39)(B).

Notice 2023-29 provides three safe harbors pursuant to which a site will be treated as a brownfield site if it is not described in 42 U.S.C. § 9601(39)(B):

1. The site was previously assessed through federal, state, territory, or federally recognized Indian tribal brownfield resources as meeting the definition of a brownfield site under 42 U.S.C. § 9601(39)(A). Potential site lists may be found under the category of “brownfields properties” on the EPA’s Cleanups in My Community webpage (https://java.epa.gov/acrespub/stvrp/).

2. An ASTM E1903 Phase II Environmental Site Assessment has been completed with respect to the site in accordance with the most current applicable version of the Standard Practice for Environmental Site

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Assessments: Phase II Environmental Site Assessment Process of ASTM International and such Phase II Assessment confirms the presence on the site of a hazardous substance as defined under 42 U.S.C. § 9601(14), or a pollutant or contaminant as defined under 42 U.S.C. § 9601(33).

3. For projects with a nameplate capacity of not greater than 5MW AC, an ASTM E1527 Phase I Environmental Site Assessment has been completed with respect to the site in accordance with the most current applicable version of the Standard Practice for Environmental Site Assessments: Phase I Environmental Site Assessment Process of ASTM International.

Statistical Area Category

The Statistical Area Category includes each Metropolitan Statistical Areas (MSA) and non-Metropolitan Statistical Area (non-MSA) that (1) has (or had at any time after December 31, 2009) 0.17% or greater direct employment (Fossil Fuel Employment) or 25% or greater local tax revenues (Fossil Fuel Tax Revenue) related to the extraction, processing, transport, or storage of coal, oil, or natural gas and (2) has an unemployment rate at or above the national average unemployment rate for the previous year, in each case as determined by the Secretary of the Treasury.

Appendix A of Notice 2023-29 specifies MSAs and non-MSAs that are used for all purposes of the notice and indicates that MSAs are grouped according to the standards of the Office of Management and Budget (OMB).

Fossil Fuel Employment

For determining Fossil Fuel Employment, the number of people employed in the industries identified by the 2017 North American Industry Classification System (NAICS) codes specified in Notice 2023-29 is divided by the total number of people employed in the area, in each case as specified in the annual County Files of the County Business Patterns (CBP) published by the Census Bureau. Appendix B of Notice 2023-29 lists MSAs and non-MSAs that meet the Fossil Fuel Employment requirement.

Unemployment

Notice 2023-29 provides that the Local Area Unemployment Statistics annual data for counties from the Bureau of Labor and Statistics, available at https://www.bls.gov/lau, determines the unemployment rate. Notice 2023-29 indicates that Treasury and the IRS intend to issue a listing identifying the MSAs and non-MSAs that meet the fossil fuel requirement and unemployment rate requirement after the unemployment data for 2022 becomes available in April and then update the listing annually each May. The first listing will apply to the period beginning on January 1, 2023. Each subsequent annual release will determine the MSAs and non-MSAs that meet the fossil fuel requirement and unemployment rate requirement for the period starting with the next update.

- Under this approach, it should generally be possible to determine, as of any given date, whether the unemployment test is met. However, it does raise the possibility that, for example, a facility placed in service in March of a year (before the update occurs) could be treated differently from a facility placed in service in June of the same year (after the update occurs).

Fossil Fuel Tax Revenue

Notice 2023-29 does not address energy community qualification based on Fossil Fuel Tax Revenue, instead requesting comments addressing the possible data sources, revenue categories, and procedures related to the Fossil Fuel Tax Revenue qualification.

Coal Closure Category

The Coal Closure Category includes census tracts, and census tracts directly adjoining such census tracts: (1) in which a coal mine has closed after December 31, 1999, or (2) in which a coal-fired electric generating unit has been retired after December 31, 2009. The term "census tract" is defined by the Census Bureau for purposes of the 2020 Decennial Census. Notice 2023-29 helpfully clarifies that census tracts are treated as directly adjoining if their boundaries touch at any single point.

The term "closed coal mine" means a coal mine classified as a surface or underground mine that has ever had for any period of time, since December 31, 1999, a mine status of abandoned or abandoned and sealed by the U.S. Department of Labor's Mine Safety and Health Administration (MSHA) in the Mine Data Retrieval System (MDRS).

The term "retired coal-fired electric generating unit" means an electric generating unit classified as retired at any time since December 31, 2009 by the U.S. Energy Information Administration (EIA) of the U.S. Department of Energy in the Preliminary Monthly Electric Generator Inventory (EIA Form 860M) or the Electric Generator Inventory (EIA Form 860). When listed as retired, the generating unit must be characterized as a coal-fired electric generating unit in the EIA data. An electric generating unit is a generating unit if classified in EIA Form 860M for years 2016 to 2022 or EIA Form 860 for years 2010 to 2015. For years 2014 to 2022, coal-fired electric generating units are those listed in EIA Form 860M or EIA Form 860 data as having a "Technology" of "Conventional Steam Coal" or "Coal Integrated Gasification Combined Cycle." For years 2010 to 2013, coal-fired electric generating units are those listed in EIA Form 860 data as having a primary fuel source code of anthracite coal, bituminous coal, lignite coal, refined coal, coal-derived synthesis gas, subbituminous coal, and waste/other coal. A retirement after December 31, 2009 of a single coal-fired electric generating unit in a plant with multiple units would cause the census tract in which such retired unit is located to qualify as an energy community.

Closed coal mines and coal-fired electric generating units listed in the MSHA or EIA data are excluded from qualifying a census tract as an energy community if they have irregular location information, but taxpayers may present evidence to correct irregular location information to MSHA (for coal mines) or EIA (for coal-fired electric generating units) to address potential issues related to irregular location information.

- It remains to be seen whether Treasury and the IRS will allow taxpayers to present evidence to correct misclassifications or errors in the EIA Form 860M or EIA Form 860 reporting.

Appendix C of Notice 2023-29 lists census tracts included in the Coal Closure Category.

Location Requirement

Timing

For purposes of the PTC, energy community qualification is determined separately for each taxable year of the qualified facility's 10-year credit period, and a facility is treated as located in an energy community during a taxable year if it is located in an energy community during any part of the taxable year.

- Unless the beginning of construction rule discussed below applies, this rule will significantly weaken the incentive to locate a PTC project in an energy community because it cannot be known in advance whether the project will qualify from year to year. For such projects, the ITC may be a more beneficial incentive if the location qualifies as an energy community when the project is placed in service.

For purposes of the ITC, energy community qualification is determined when a project or energy storage technology is placed in service (*i.e.,* the date the credit is determined).

However, Notice 2023-29 provides that if a taxpayer begins construction on a facility or project in an energy community on or after January 1, 2023, then the location will continue to be considered an energy community for the duration of the credit period for the PTC or on the placed-in-service date for the ITC with respect to that facility or project. For this purpose, prior guidance interpreting the beginning of construction for purposes of the PTC and ITC will apply. See Notices 2013-29, 2013-60, 2014-46, 2015-25, 2016-31, 2017-04, 2018-59, 2019-43, and 2020-41 and 2021-41.

- This is a welcome clarification of the rule that will provide additional certainty for taxpayers. This is particularly important for PTC facilities, which otherwise cannot be certain to qualify for the energy community enhancement from year to year.

- A prior version of the notice did not include the "on or after January 1, 2023" limitation. The added limitation is unfortunate and seems to penalize taxpayers who started construction too early. The limitation raises particularly difficult issues for taxpayers who undertook physical work at the end of 2022 and the beginning of 2023 with the goal of beginning construction on or before the January 28 deadline to eliminate the need to demonstrate compliance with the prevailing wage and apprenticeship requirements. Now these taxpayers must determine whether construction began in 2022 (in which case the energy community "beginning of construction" rule would not be available) or 2023 (in which case the energy community "beginning of construction" would be available). It is unclear what policy objectives are served by this limitation.

Nameplate Capacity Test

A project or facility that has a nameplate capacity is considered located in or placed in service within an energy community if 50% or more of its nameplate capacity in MW (consisting of energy-generating units) is in an energy community. Nameplate capacity for an electrical generating unit means the maximum electrical generating output that the unit is capable of producing on a steady-state basis and during continuous operation under standard conditions, as measured by the manufacturer and consistent with the definition provided in 40 CFR § 96.202. Energy-generating units that generate direct current (DC) before converting to alternating current (AC) (*e.g.,* solar

photovoltaic panels) should use the nameplate capacity in DC; otherwise, the nameplate capacity in AC should be used. For energy storage devices, the nameplate or maximum rated capacity means electric storage device capacity (in MW) multiplied by the duration hours of that storage capacity (h).

If a facility or project with offshore energy generation units has nameplate capacity but none of the applicable energy-generating units are in a census tract, MSA, or non-MSA, then the Capacity Test for such facility or project is applied by attributing all the nameplate capacity of such facility or project to the land-based power conditioning equipment that conditions energy generated by the facility or project for transmission, distribution, or use and that is closest to the point of interconnection.

Footprint Test

A project or facility that does not have a nameplate capacity (*e.g.,* qualified biogas property) is considered located in or placed in service within an energy community if 50% or more of its square footage is in an area that qualifies as an energy community.

Summary

Notice 2023-29 is timely. For the past several months, transactions involving projects with potential energy community enhancements have included complex provisions addressing the circumstances under which prices or terms would be adjusted to take into account the energy community enhancement. Notice 2023-29 should render many of these provisions moot. In addition, Notice 2023-29 provides straightforward, easy-to-apply rules for many, though by no means all, of the legal questions raised by the statute; the Appendices take that approach a step further by providing comprehensive lists of relevant concepts. As a result, for many projects, Notice 2023-29 should greatly simplify the determination of whether property is located in an energy community.

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