



July 11, 2023

**ATTORNEY WORK PRODUCT**

**To:** Tribal Energy Clients  
**From:** Pilar M. Thomas  
**Re:** Summary of Inflation Reduction Act Provisions Related to Elective Payments for Tax Credits: Implications and Considerations for Tribes

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As we have previously advised, the Treasury and Internal Revenue Service (IRS) have issued proposed rules to implement Section 6417 of the Inflation Reduction Act (IRA). Section 6417 amends the Internal Revenue Code (Code) to authorize “applicable entities” to elect to receive a payment (“Elective Pay” – aka “Direct Pay”) from the IRS equal to the amount of various clean energy tax credits also authorized under the IRA. The proposed rules implement Section 6417 and address several issues of key relevance to Indian tribes.

Treasury will hold tribal consultation on Monday, July 17 to address several questions posed to tribes in its Tribal Leader Letter (attached). In addition, written comments are due August 18. Treasury will also hold a public hearing on August 21.

This memorandum summarizes the most relevant aspects of the proposed rules, discusses implications for tribes’ efforts to deploy clean energy projects and technologies, and proposes potential comments for the upcoming tribal consultation and the comment period.

**Summary of Proposed Rule**

The proposed rule addresses several implementation aspects of the “Elective Pay” provision, including:

- Definitions of “applicable entity”
- Determination of “applicable credit”
- Project ownership and ownership structures
- Transferability of elective payments
- Use of grant funds or tax exempt financing
- Registration requirements
- Tax return requirements

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Definition of “Applicable Entity.” Section 6417 defines applicable entity to include “Indian tribal governments.” Treasury proposes to expand this term to include tribal government agencies, instrumentalities, and political subdivisions. This expansion will treat tribes similarly to state governments. The examples used are tribal utilities, housing authorities, energy authorities or departments. Treasury is taking comment on whether the term should also include tribal enterprises, including those owned in part by tribal governments.

Determination of “Applicable Credit.” Tax credits will be determined based on the relevant provisions for tax credits (primarily Sections 30, 45, and 48). Bonus credits, such as for the Low-Income Community Bonus Credit Program (an additional 10% or 20%), are also applicable credits. Thus, tax credit rates can range from 6% to 70%. The amount of the credit will also be adjusted based on other limitations in the Code, including Section 49 (which limits the credit based on use of non-recourse, non-qualified financing).

Project Ownership and Structures. Treasury has confirmed that projects must be owned by the applicable entity to be eligible for Elective Pay. This ownership can be direct or through disregarded entities (such as sole member LLC). If the property/project is owned by a disregarded entity, the applicable entity member will claim the tax credit. In addition, applicable entities can co-own projects, through “unincorporated joint ventures” such as tenancy-in-common or joint operating agreements, with other applicable entities or taxable entities. In such joint ownership structures, the applicable entity will claim its share of the tax credit. Treasury has included special rules for these circumstances. However, applicable entities cannot co-own projects through partnerships or S corporation structures. Treasury is taking further comment on joint ownership structures.

Transferability of Elective Payment. Treasury has taken the position that an applicable entity cannot buy tax credits from an eligible taxpayer under the transferability provisions in Section 6418, and then claim those tax credits through the elective payment. Treasury is also prohibiting “lessor/lessee” arrangements (presumably sale-lease backs or inverted leases). This is grounded in Treasury’s position that the applicable entity has to have an ownership interest in the property/project. However, Treasury is taking comment on whether transferability should be allowed under certain circumstances.

Treatment of Grant Income. The proposed rule includes special rules related to the treatment of grants and tax-exempt financing to determine the basis for tax credits. The current rule is that the basis is reduced by the amount of tax-exempt grants or financing. However, since all grants to applicable entities are tax-exempt, Treasury has concluded that the current rule should not apply as they would frustrate the purposes of the Elective Pay provision. Therefore, certain property/projects that are purchased or constructed using grant funds (whether federal, state or private) will not have their basis reduced by

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the amount of such grants. This will only apply to the ITC (investment tax credit), PTC (renewable electricity production tax credit), commercial electric vehicles, and alternative fuel/electric vehicle charging stations.

For example, if a tribe develops a 2 MW solar project for a tribal housing project – and the project qualifies for all possible tax credits (70%) and receives a \$3 million grant:

Project Cost	=	\$10 million
Tax Credit	=	\$ 7 million
Grant	=	\$ 3 million
Net Cost	=	\$ 0

However, if the total amount of the grant and the tax credit exceeds the cost of the project (i.e., the grant amount is \$ 4 million or more in this example), then the amount of the tax credit will be reduced so that the total is not more than the project cost. Note, grant information will have to be reported during the registration process, discussed below.

Pre-Filing Registration. In order to receive an Elective Payment, an applicable entity must register itself and its property/projects to claim the applicable tax credits. To register, the applicable entity must provide information for each project, including: entity name, tax year, applicable credits expected to claim, when the project(s) were placed into service, when started construction on the project(s), and whether grant funds were used. Treasury will provide a registration number for the applicable entity and one for each project. The registration number(s) must be included on the required tax return.

Tax Returns. Treasury recognizes that state, tribal and local governments (and their agencies, instrumentalities and political subdivisions) are not required to file tax returns, but Treasury will require these applicable entities to file a Form 990-T and Form 3800 to be able to claim the tax credits and make the election to receive their payment. A Form 990-T is an informational return, typically filed by tax-exempt organizations for unrelated business income. The Form 3800 is used to claim General Business Credits, including the investment tax credit and production tax credits for energy projects. Tax returns will be due on the 15<sup>th</sup> day of the fifth month after the end of the entity's tax year. The Elective Pay must be claimed on the original tax return (it cannot be claimed on an amended return). The amount claimed will be cumulative for all the projects placed into operation during the tax year. The Elective Payment is irrevocable.

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### **Tribal Consultation and Other Treasury Requests for Comments**

For tribal consultation purposes, Treasury has specifically requested comments on:

- Whether to include tribal enterprises, regardless of how chartered or whether partially owned, or other entity structures used for energy projects in the definition of Indian tribal governments
- Pre-filing registration requirements

Treasury has also requested public comments on:

- Including agencies, instrumentalities or political subdivisions for all governments in defining applicable entities
- Additional rules and treatment for disregarded entities, undivided ownership interests, and partnerships.
- Applicability of Section 49 to determine tax credit amount
- Limited situations to allow for an “elective payment” of transferred tax credits.

### **Other Considerations for Tribal Comments**

The proposed rules raise several other questions and considerations for tribal governments and enterprises. In particular, tribes might want to comment on the following:

- Section 17s are typically treated by the IRS as “arms of the tribe” so Treasury should clarify that Section 17 companies are applicable entities.
- Treasury is already seeking comment on whether tribally-chartered tribal-owned enterprises should be non-taxable. In addition, Treasury has proposed that tribal enterprises are eligible to own projects under the Low-Income Community Bonus Credit Program. Treasury and the IRS should harmonize all three of these efforts – to the benefit of tribes.
- Some tribes want to partner with others to develop, finance and own clean energy projects – especially commercial scale projects. As previously commented, Treasury should allow the project sponsors (the tribe and its partner(s)) to form special purpose vehicles under an LLC structure. This is common for public-private partnership infrastructure projects. It is unclear that a tenancy-in-common can be structured for projects on tribal lands, given the trust status of the real property.
- Since tribes cannot monetize their Elective Payments through transferability, they should be able to structure projects through sale-leasebacks or inverted leases – which would allow tribes to retain ownership of the project, while a third-party receives the tax benefits in exchange for contributing capital to the project.
- Clarify whether the application of Section 49 to limit the tax credits should apply to applicable entities that are eligible for federal loan guarantee programs. Also, are direct

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loan programs – such as the United States Department of Agriculture’s Rural Utilities Service and the United States Department of Energy – considered non-recourse non-qualified financings?

- Clarify if a tribe has to register every year it intends to claim a tax credit. The registration is at the entity and project level. Do tribes renew the entity registration?
- Clarify how governments will complete the Form 990-T tax return, such as what information is relevant or necessary. For example, if the tribe owns a project that generates revenue, does this have to be reported?
- How do tribes determine their tax year – is it based on their fiscal year or calendar year? Do tribes have a choice?

Please feel free to contact me if you have any further questions about the proposed rules for Elective Payments. If your tribe is interested in participating in the tribal consultation and/or submitting comments, we’re happy to assist with drafting talking points or comments.