

Lawyer Insights

IRA solar tax credit transfers explained for companies with low (or no) tax liability

By Laura Jones and Jason Eisenberg
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The [Inflation Reduction Act \(IRA\) significantly altered](#) the landscape for the transferability of energy tax credits. The IRA added Section 6418 to the Internal Revenue Code, which permits eligible taxpayers (transferors) to transfer (sell) certain renewable energy tax credits to unrelated taxpayers (transferees) for cash. The following 11 tax credits may be transferred under Section 6418:

- Section 30C (alternative fuel vehicle refueling property)
- Section 45 (renewable electricity production)
- Section 45Q (carbon oxide sequestration)
- Section 45U (zero-emission nuclear power production)
- Section 45V (clean hydrogen production)
- Section 45X (advance manufacturing production)
- Section 45Y (clean electricity production)
- Section 45Z (clean fuel production)
- Section 48 (energy investment)
- Section 48C (qualifying advanced energy project investment)
- Section 48E (clean electricity investment)

Issues with pre-IRA tax credits | Prior to the IRA, these credits could not be transferred. Renewable energy companies with low tax liabilities instead had to find investor partners and use complicated, costly transaction structures involving substantial risk and due diligence to monetize tax credits. Such amounts of risk and diligence, generally, are not feasible for smaller developers. Section 6418 gives renewable energy companies with low tax liabilities an easier path to take advantage of these tax credits.

Section 6418 tax credit transfers provide nontaxable opportunities to sell and purchase tax credits. Any cash paid for the transferred credit is not included in the transferor's gross income and is not deductible by the transferee. The transferee may use the transferred credit in full without including any discount (i.e., the difference between the cash paid for the credit and the amount of tax credits) in the transferee's gross income. This allows renewable energy companies without sufficient tax liability to generate and sell tax credits tax-free at 85% to 95% of the credit's amount, without the need for traditional tax equity transaction structures.

On June 14, 2023, the Department of the Treasury and the Internal Revenue Service (IRS) issued

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1. proposed regulations regarding Section 6418 tax credit transfers, and
2. temporary regulations regarding pre-filing registration requirements for such transfers.

The IRS also posted Frequently Asked Questions regarding such transfers. Here is an overview of the proposed and temporary regulations as well as the remaining challenges.

Proposed regulations

Transferable credits include any bonus credit amounts (i.e., domestic content, energy communities, etc.). However, a transferor is not permitted to transfer only the “bonus” credit amount separately from the “base” credit amount — instead, any transferred portion must reflect a proportionate share of the bonus and base credit amounts.

Any amounts paid by a transferee taxpayer in connection with the transfer of a credit must be paid in cash (which includes checks, cashier’s checks, money orders, wire transfers, ACH transfers, and other bank transfers of immediately available funds) within the period beginning on the first day of the transferor’s taxable year during which the applicable credit is determined and ending on the earlier of the filing of the transferor or transferee tax return.

Certain advanced commitments to purchase credits are allowed, however, the actual payments must be made in the window described above. Future guidance allowing advanced commitments together with substantial prepayments will be crucial for smaller developers to effectively monetize streams of tax credits (such as Section 45 PTCs).

A transfer election must be made for each “single eligible credit property.” A taxpayer may retain a portion of the credit and transfer the balance and/or make multiple elections to transfer portions of the credit to multiple transferees. For credits claimed over several years (e.g., the Section 45 PTC), an election must be made for each taxable year of the credit period. Future guidance may clarify if group elections will be permitted for projects consisting of several single eligible credit properties (i.e., allowing a single transfer election for all wind turbines in a wind farm).

A transfer election is irrevocable, and second transfers of credits are prohibited. Pooling or dealer arrangements would violate the second transfer prohibition, but a broker arrangement matching potential buyers and sellers of credits is fine as long as the credits are not treated as transferred to the broker under general tax ownership principles.

Any recapture amount is taken into account by the transferee. The transferor and transferee may contract for indemnification in the event of a recapture event. In addition, tax indemnity insurance may be available to cover any recapture tax credits due to a casualty event. Transferees may also be subject to a 20% penalty for excessive credit transfers, but a recapture event is not deemed to be an excessive credit transfer.

Note that, under the proposed regulations, purchased credits are still subject to the passive activity rules. Accordingly, only individuals and closely held corporations (i.e., family businesses) with passive income are able to purchase and utilize the tax credits.

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Temporary regulations

Taxpayers are required to register before filing the tax return on which a transfer election is made and provide certain information on a transfer election statement related to each property. The transferor is also required to provide the transferee with certain required minimum documentation. The registration is only valid for the taxable year the credit is determined for the property and for a transferee's taxable year in which the credit is taken into account. If credits will be claimed in a taxable year after a registration number has been obtained, the registration must be renewed by the taxpayer, including attesting that no information has changed or, if it has, updating the information.

The proposed and temporary regulations provide much-awaited guidance to taxpayers that have been waiting to execute or close on tax credit transfer transactions. While the proposed regulations answer many outstanding questions, several issues are not fully addressed. One key remaining issue is the scope of the IRS pre-filing review process and the IRS's audit procedures following the filing of the relevant transferor and transferee tax returns and forms.

Potential for tax credit rollbacks

Due to the partisan divide over the IRA, current mixed governance and the potential transfer of power after the 2024 elections, tax credit rollbacks are possible. However, recent Republican efforts to rollback IRA provisions have related primarily to only a few Section 6418 credits (the Section 45Y and 48E clean electricity credits), and not larger IRA repeal efforts (such as the repeal efforts that occurred in the debt-limit negotiations earlier this year). Republicans are also disincentivized to repeal major IRA provisions, as two-thirds of the major clean energy projects announced since the IRA's passage are located in Republican-controlled districts.

Related tax credits and future guidance

Guidance is currently anticipated for several of the transfer eligible tax credits. Additionally, clarifications and final regulations are yet to be issued for tax credit transfers, bonus credits and prevailing wage and apprenticeship requirements. The Treasury recently announced that guidance on the Section 45X and Section 48 tax credits will be issued by the end of 2024.

Any guidance that will impact the ability to qualify and claim the eligible tax credits will likely also impact the transferability of tax credits. The risks of entering into tax credit transfer transactions can be mitigated by contracting for indemnities and releases in the event of unfavorable guidance.

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