Practical Implementation of the Inflation Reduction Act

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Agenda

I. Introduction to Inflation Reduction Act (“IRA”), Eligible Projects & Timing
II. Tax Credits
III. Considerations, Project Timeline & Funding Options
IV. Questions

Introduction to Inflation Reduction Act ("IRA"), Eligible Projects & Timing Considerations

Introduction to the Inflation Reduction Act ("IRA")

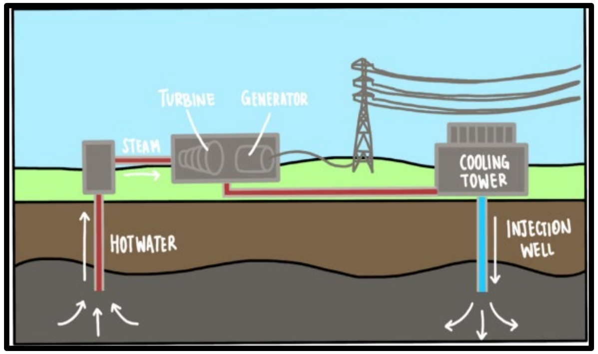
IRA is the largest investment in U.S. Energy Infrastructure, with varied incentives to help subsidize the cost of achieving environmental goals.

- Signed into law on August 16th, 2022
- Provides **$369 billion over the next decade** for new & existing programs
- Goal of **reducing emissions by ~40% by 2030**
- Potential for **tax incentives** to touch multiple aspects of communities
- The U.S. Treasury is in the process of developing detailed guidance, processes, & forms for each of the credits

Sources:; https://www.congress.gov/bill/117th-congress/house-bill/3684/text; Inflation Reduction Act, Pub. L. No. 117-169, 136 Stat. 1818 (2022),

Eligible Projects under IRA

- Installation of **energy facilities**
  - Solar
  - Wind
  - Microgrid
  - Biogas
- Energy **efficient building** design & construction
  - Thermal
  - Geothermal
- Conversion of **vehicle fleets** to electric/hybrid
- Electric Vehicle (EV) deployment to include the **charging station** network



Sources:; https://www.congress.gov/bill/117th-congress/house-bill/3684/text; Inflation Reduction Act, Pub. L. No. 117-169, 136 Stat. 1818 (2022),

IRA Timing Considerations

- Consider accelerating projects because over time, certain incentives stop and / or become more restrictive
- The prevailing wage and apprenticeship provisions become operative for facilities when construction begins on or after January 30, 2023

January 1, 2023	EV charging station tax credit only applies to low income & rural areas
December 31, 2024	Alternative Fuel Excise tax credit expires
December 31, 2024	Deadline for beginning construction on projects for Renewable Energy Facilities tax credit
January 1, 2025	New provisions apply for Renewable Energy facilities; zero GHG emissions required; domestic content requirements
December 31, 2031	Energy Efficient Commercial Building Deduction expires
December 31, 2032	EV Charging Station tax credit expires
December 31, 2033	Deadline for vehicles placed in service for Qualified Commercial Clean Vehicle tax credit

Sources: Inflation Reduction Act, Congressional Research Service, "Tax Provisions in the Inflation Reduction Act of 2022", August 10, 2022; https://crsreports.congress.gov/product/pdf/R/R47202; https://home.treasury.gov/system/files/136/Fact-Sheet-IRA-Equitable-Clean-Energy-Economy.pdf

Direct Ownership Alternative, Power Purchase Agreement (PPA)

- PPA is standard legal agreement between property owner and third party whereby the third party finances up-front costs of installation and maintenance of solar system on owner's property.
- The term can be up to 25 years

Third Party Developer

- Finances design, installation, maintenance, and insurance
- Sells solar energy to school district for duration of contract
- Benefit: Retains federal credits and depreciation benefits
- Benefit: Receives energy costs savings + political capital of on-site solar power generation

School District

- Buys solar energy from developer produced by system at lower price than utility power
- Includes cost inflation over duration of contract
- Benefit: Provides certainty in budgeting
- Benefit: Mitigates risk associated with owning solar assets

Direct Pay Tax Credits

Changes to Tax Incentives

- Previously, renewable incentives only available to tax-paying entities; **now tax-exempt entities can benefit from incentives directly**
- In many cases, existing incentives **increased** and/or **extended**
- New incentives **added**
- **Cost of achieving environmental objectives likely lower** now than prior to the IRA
- Projects **constructed in 2022 could be eligible** depending on when project reaches commercial operation

Sample Increased and/or Extended Incentives

- Expanded and modified "179D" tax deduction for energy efficiency in commercial buildings
- Expanded Production Tax Credit to include solar (previously expired 2005)
- Extended the Production Tax Credit & Investment Tax Credit to 2032 for carbon neutral technologies
- Increased credit for EV charging stations from $30,000 to $100,000 & modified definition from "per location" to "per unit"

Sample New Incentive

- Added Commercial Clean Vehicle Credit: Provides up to $40,000 subsidy for large vehicle replacement (> 7 tons)

Sources: Infrastructure Investment and Jobs Act, Pub. L. No. 117-58, 135 Stat. 429 (2021), https://www.congress.gov/bill/117thcongress/housebill/3684/text/pl'; Inflation Reduction Act, Pub. L. No. 117-169, 136 Stat. 1818 (2022), https://www.congress.gov/bill/117th-congress/house-bill/5376

IRA Tax Incentives & Transformational Initiatives

There are several tax incentives within the IRA that could lower the cost of transforming to a greener, less carbon-intensive footprint

- Most incentives available in form of **direct payment** from U.S. Treasury, following project completion or acquisition
- Tax incentives available to **all eligible projects**; no competitive process for receiving the subsidy
- Projects will likely have to be registered (not active yet)
- Potential advantages to accelerating projects before incentives expire or requirements become more stringent
- Incentives for technologies ranging from electrification of vehicle fleets to improvements to buildings to the development of manufacturing facilities

Tax Incentives for Tax-Exempt Entities

- Incentives available to tax-exempt entities primarily take form of a direct payment from U.S. Treasury
  - One-time direct payment on reimbursement basis for qualified costs
  - **Investment Tax Credit** (ITC): upfront subsidy of project costs for renewable energy

    OR

  - **Production Tax Credit** (PTC), subsidy over time based on power generated
- The IRA contains "gross-up" provision to prevent direct-pay subsidies from being reduced under budget sequestration rules
- For energy efficiency projects in buildings, tax credit takes form of deduction that can potentially be traded to business partner

Sources: Inflation Reduction Act, Congressional Research Service, "Tax Provisions in the Inflation Reduction Act of 2022", August 10, 2022; https://crsreports.congress.gov/product/pdf/R/R47202; https://home.treasury.gov/system/files/136/Fact-Sheet-IRA-Equitable-Clean-Energy-Economy.pdf

Key Provisions of the Tax Incentives Enhance the Base Incentive

- The Investment Tax Credit includes **domestic content requirements** that decrease over time

- The **energy community requirement** applies to communities that have above average unemployment from coal or natural gas employment reduction

- For certain tax incentive programs & projects[1], there are opportunities to significantly enhance the base benefit (i.e., by five times) by:
  - Paying a **Fair Wage** (i.e., Davis-Bacon Act)
  - Meeting **Apprenticeship** Requirements

  (1) Projects under 1MWh are exempt from prevailing wage and apprenticeship requirements

- **15%** "haircut" if tax-exempt financing is used

6% Base

+ 2% Meets Domestic Content Requirements

+ 2% Meets Energy Community Requirements

x5 Meets Prevailing Wage & Apprenticeship

less 15% of credit if Financed through Tax-Exempt Bonds

Total Potential Credit Value is 6% - 50%

Sources: Inflation Reduction Act, Pub. L. No. 117-169, 136 Stat. 1818 (2022), https://www.congress.gov/bill/117th-congress/house-bill/5376/text;The White House "Building a Clean Energy Economy: A Guidebook to the Inflation Reduction Act's Investments in Clean Energy and Climate Action," December 2022, Version 1; IRS Notice 2022-61

Sample Tax Incentive

- A typical example of an Investment Tax Credit computation is shown below:

6% Base Credit for Qualifying Energy Projects

X5 Meets Prevailing Wage & Apprenticeship*

Less 15% of credit if Financed through Tax-Exempt Bonds

Example for $5 million project

6%, or $300,000	**6% X 5 = 30% or $1,500,000**	**30% * -15% = 25.5% or $1,275,000**

** Projects under 1 MWh are exempt from the Fair Wage & Apprenticeship Requirements.*

Sources: Inflation Reduction Act, Pub. L. No. 117-169, 136 Stat. 1818 (2022), https://www.congress.gov/bill/117th-congress/house-bill/5376/text;The White House "Building a Clean Energy Economy: A Guidebook to the Inflation Reduction Act's Investments in Clean Energy and Climate Action," December 2022, Version 1; IRS Notice 2022-61

Example: Comparison of Solar Financing Alternatives

- The sample below illustrates potential savings on a solar project:

	Prior to the IRA, District Ownership	PTC, Finance with Taxable Debt	ITC, Finance with Taxable Debt	ITC, Finance with Tax-Exempt Debt
		PTC	**ITC**	**ITC**
5MW Solar, Upfront Cost	$5 million	$5 million	$5 million	$5 million
Reimbursement Rate from IRS	None	$26/MWh	30%	25.5%
Reimbursement Amount from IRS*	None	$1.810 million	$1.425 million	$1.211 million
Net Upfront Cost	$5.0 million	$5.0 million	$3.575 million	$3.789 million
Net Present Value of Debt Service on Bonds*	**$5.12 million**	**$3.83 million**	**$3.88 million**	**$3.69 million**
Average Debt Service Cost per MWh	$3.178	Years 1-10: $1.45 Thereafter: $3.24	$2.409	$2.288

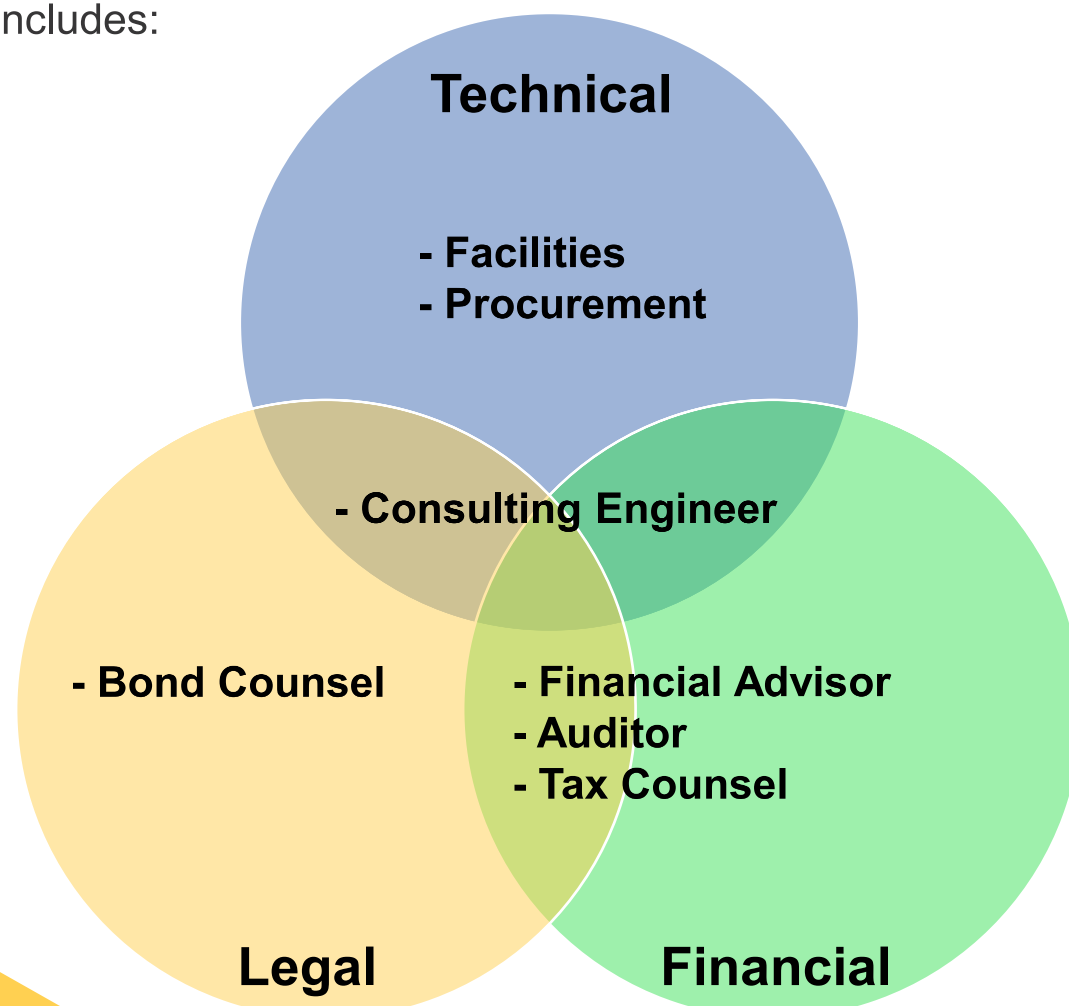
- Key Assumptions:
  - District meets Fair Wage & Apprenticeship requirements; no bonus credits
  - Investment Tax Credit (ITC) assumes 95% of total costs are qualified costs
  - Production Tax Credits assume 24.5% capacity factor, 0.5% annual degradation factor
  - Construction begins by December 31, 2024
  - Debt service cost estimated with financing over 20 years with level annual debt service payments. Present valued at 4%.

Not reflective of an actual project, for Illustration Purposes Only

Considerations & Funding Options

Assembling the District's Team to Evaluate the District's Options

- We generally recommend establishing a "Due Diligence Team" to review these opportunities as well as evolving guidance from US Treasury.
- Composition includes:



Considerations

- **Identify & evaluate IRA incentives** that may support District's own environmental objectives.
  - For solar (or wind, microgrid or biogas) projects:
    - Compare Power Purchase Agreements to direct ownership
    - Compare Investment Tax Credit vs. Production Tax Credit
    - Compare financial impact of using tax-exempt debt & lower incentive vs. taxable debt & higher incentive
  - For projects under construction, determine eligibility & track eligible costs for reimbursement (accountant attestation)
  - Identify location of "energy communities" in area, if any
- **Accelerating** certain programs or projects in light of step-down in incentives or more stringent requirements
- **Adding** programs or projects in light of incentives available
- Programs across departments to try to capture as many of incentives as possible
  - Identify opportunities to combine credits & increase credits
  - Identify any overlap in IRA & IIJA incentives
- **Awareness campaign** for incentives available to residents & businesses
- Review of grant funding and national green bank opportunities in IRA (not covered in this presentation)

PPA vs. Direct Ownership Process Comparison

PPA	Process	Direct Ownership
Handled by developer	Design/Engineering	Hire the architect and construction manager to design
Developer to manage	Construction / Procurement	Responsibility to design the system
Take or pay financing	Financing	Various options outlined in following slides
Power delivery to meter	Operation	Must budget for any long-term operational costs
Costs related to hosting developer on property / built into fee structure of PPA	Maintenance	Use own employees or hire third-party to maintain (relevant to compliance with manufacturer's warranty)
Developer	End-recipient of potential tax credit(s)	District

Potential IRA Project Timeline

Plan

- Determine potential projects
- Work with the District's team (CM, Architect, Bond Counsel, Municipal Advisor) to identify which projects are IRA tax credit eligible
- Evaluate the projects and calculate the amount of the tax credit

Pre-Authorize

- Complete necessary forms to get projects pre-authorized
- Department of Treasury is still working on final version, but pre-authorization is necessary to get tax credit
- Determine bidding parameters
- Obtain Board Approval

Construct

- Include IRA tax credit provisions in RFPs and bidding documents
- Retain records and documentation for IRA (prevailing wage and apprenticeship, if needed)

Tax Credit

- Submit final forms to Treasury
- Receive tax credit reimbursement year following completion of project

Funding Options

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	Unlimited Tax Bonds	Limited Tax Bonds	Energy Conservation Bonds (LT)	Sinking Fund Revenue	Fund Balance
Advantages	• Dedicated debt millage covers annual debt payments • School captures all energy savings	• Not subject to voter approval	• Not subject to voter approval • Not subject to 5% SEV non-voted debt limit	• Sinking Fund millage revenue covers costs of project • No financing expenses or interest cost	• Not subject to voter approval • No financing expenses or interest cost
Disadvantages	• Subject to voter approval • Possible added time and cost of an election • Cost of issuance and interest cost	• Annual debt payments paid from general fund or sinking fund • Cost of issuance and interest cost	• Annual debt payments paid from general fund or sinking fund • State reporting requirements • Cost of issuance and interest cost	• Fund availability is subject to collection of sinking fund revenue • Potential loss of future interest earnings	• Funds for project from general fund or capital improvement fund • Potential loss of future interest earnings
Limitations	• Projects need to fit into the ballot language	• Subject to 5% SEV non-voted debt limit	• Projects must be approved conversation energy projects under the Act	• Is the Project sinking fund eligible? • Reduces sinking fund revenue for other sinking fund projects	• Project cost would reduce fund balance

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Non-Voted Limited Tax General Obligation Bonds

- No voter approval required
- Debt service payable from operating funds
  - Energy projects financed are expected to produce annual savings sufficient to meet annual debt payments
- District may not transfer more than 20% of its annual state aid payments to its capital projects fund or its debt retirement fund
- Not eligible to participate in School Loan Revolving Fund
- 5% of SEV debt limit
  - Total Bonded Debt Outstanding includes all voted and non-voted debt
  - Energy bonds are exempt from the 5% Legal Debt Limitation computation

Sample Calculation – Non Voted Bonds

	2023 SEV	Est. 2024 SEV[1]	Est. 2025 SEV[1]
District's 2023 State Equalized Value (SEV)	$997,518,973	$1,047,394,922	$1,099,764,668
5% of Current State Equalized Value	49,875,949	52,369,746	54,988,233
Outstanding debt:	10,080,000	8,065,000	6,120,000
Est. Legal debt capacity for LTGO issuance	**$39,795,949**	**$44,304,746**	**$48,868,233**

[1] *Assumes 5% growth in SEV year-over-year*

Board Communication

- Introduction to Plan
  - What / Why / Where
    - Articulate your goal / purpose
    - Roof or ground mounted
    - Student involvement
  - How
    - District ownership v. Power Purchase Agreement
  - Who
    - The team – financial, legal, and other experts
  - When
    - Overall timeline
  - Parameters Defining Success

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