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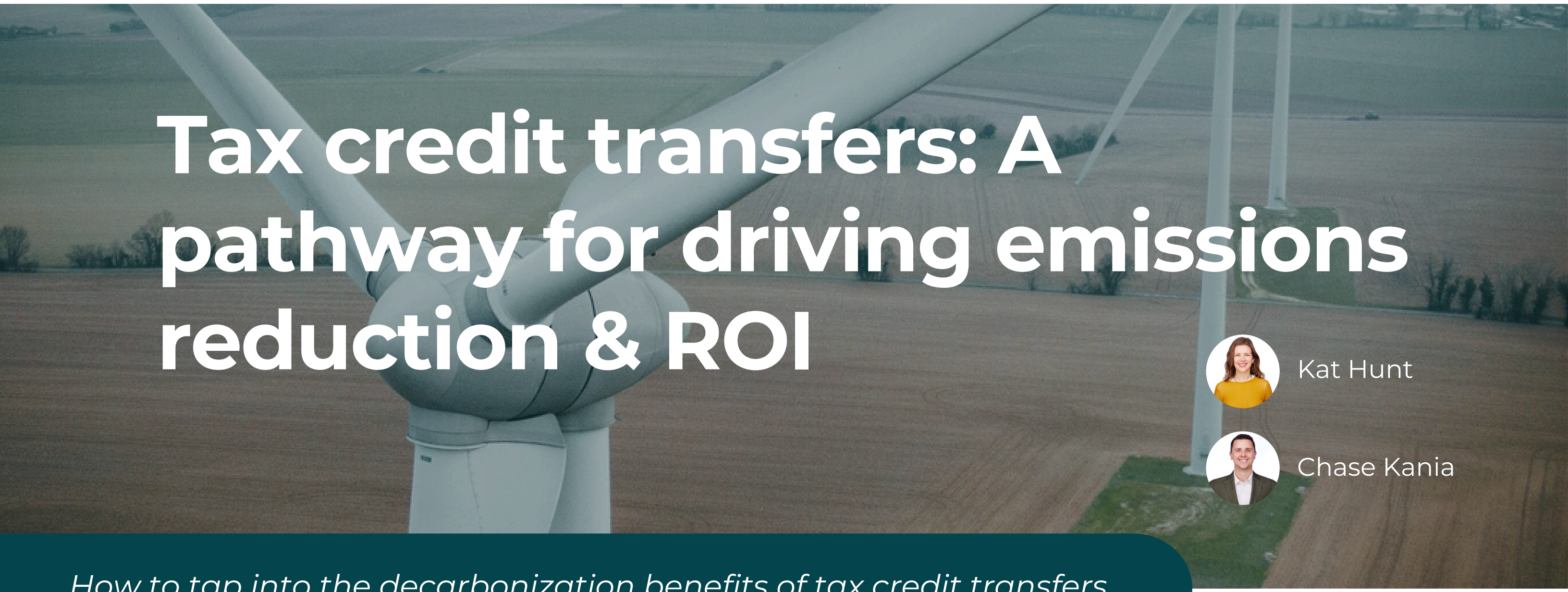

Tax credit transfers: A pathway for driving emissions reduction & ROI

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How to tap into the decarbonization benefits of tax credit transfers

Corporate spending on renewable energy and other climate transition projects has boomed in recent years, but we still have a long way to go. Climate finance needs to increase to between **$9 and $12 trillion** per year by 2050, up from the $1.8 trillion spent in 2023, to align with the Paris Agreement.

Figuring out how to finance the transition is no easy task. Tax equity – generated by government tax credits – has been a key part of renewable project finance alongside more traditional mechanisms like investor equity and debt models. The tax equity process helps producers (sellers) monetize tax credits from renewable energy projects and offers considerable tax savings for corporate buyers.

However, tax equity transactions often require complex partnership structures and significant up-front coordination. As a result, tax equity has been inaccessible to many corporate buyers – capital flows have primarily come from a handful of large lending institutions.

All that changed with the passing of the Inflation Reduction Act of 2022 (H.R. 5376). Thanks to the IRA, tax credits can be transferred to another party once generated, opening the marketplace to smaller deals, simpler transactions, and new sellers and buyers.

The tax credit transfer marketplace is expected to provide over $1.2 trillion in incentives by 2032 and nearly $50 billion of credits in 2024 alone.

The benefits aren't just financial – read on to learn how tax credit transfers work, why they can be such an effective tool for driving direct emissions reductions, and how to use them.

Want to explore transition finance mechanisms in more depth? Learn 3 ways to finance your climate transition plan.

All about tax credit transfers

Tax credit transfers allow any company with a tax liability to negotiate a simple sales agreement to purchase tax credits – often marketed at a discounted rate – to save on their U.S. Federal tax bill and finance their climate transition.

Let's say you're a corporation with a **$100 million** U.S. Federal tax liability:

- You agree to buy **$10 million** of tax credits from an energy developer or producer involved in an eligible clean energy project.
- You buy these tax credits for **90 cents on the dollar** – in other words, you've paid $9 million for $10 million in credits.
- This transaction **reduces your tax liability** from $100 million to $90 million.
- You've generated $10 million in **federal tax savings**, yielding a **simple ROI of 11%**.

While the tax credit transfer savings can be used to fund any corporate initiative or simply added to your balance sheet, you can unlock additional ROI and return on carbon (ROC) benefits by using the proceeds to further your sustainability goals. For example, you can use the proceeds to seed a green revolving fund, launch a climate innovation accelerator, or pilot supplier decarbonization initiatives that accelerate your climate transition.

The IRA is great for sellers, too – any entity without a tax liability, such as a ClimateTech startup working in clean fuels, can monetize credits to bolster cash flow and help scale their innovative technologies.

Keep in mind that only certain projects are eligible for tax credits. The IRA is designed to spur investments in climate action and clean energy. As part of the legislation, the IRA added tax credit provisions for hydrogen and energy storage and expanded or modified 11 transferable clean energy tax credits across the following categories:

- Renewable energy generation
- Carbon sequestration
- Clean fuels
- Manufacturing
- Clean vehicles

Learn more about how base credits are calculated and who can receive them here.

Tax credit transfers as a vehicle for decarbonization

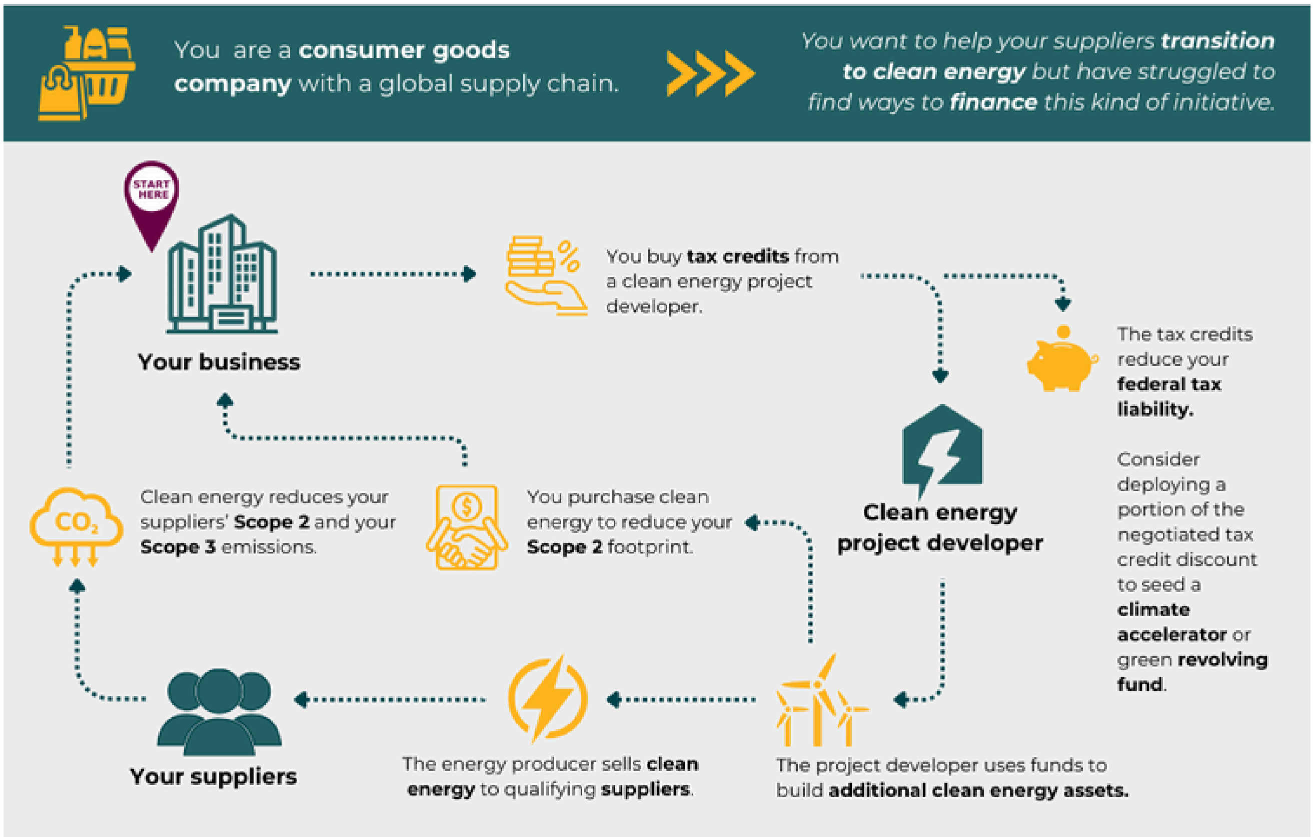
On top of the ROI and tax-saving benefits, tax credit transfers open the door for creative partnership and financing structures that allow you to fund your own transition and support high-impact decarbonization initiatives in your supply chain.

Today, if your business wanted to tackle its Scope 2 emissions, your impact would be limited by how quickly the grid transitions to clean energy or your ability to procure clean energy. With tax credit transfers, you can directly finance the development of long-term clean energy assets that reduce your Scope 2 footprint.

Or, you can distribute clean energy to qualified suppliers to help them reduce their Scope 2 footprint, which in turn reduces your Scope 3 footprint. You can even offer suppliers a forward commitment for credit purchases if they install onsite solar generation systems, allowing you and your suppliers to tap into the ROI and ROC benefits of tax credit transfers.

> Tax credit transfers can be tailored to the size and scale of action needed, making them a great way to fund expensive, high-impact initiatives like supplier clean energy transition and other value chain programs.

Here's an example of how tax credit transferability can boost ROI and ROC for you and your suppliers:



Key considerations

Transferability makes the tax credit market more accessible to smaller buyers by reducing the "soft costs" of pre-IRA tax equity (legal, accounting, diligence, contracting, etc.). However, these aren't riskless transactions.

The requirements around base credits, adder credits, and prevailing wage and apprenticeship require robust due diligence. You'll need a partner to help you vet potential projects, negotiate insurance and indemnification protections, and even ensure the transaction itself.

Additionally, there are still transaction fees. If your tax liability is relatively small (say less than $5 million), you'll need to find ways to reduce your costs to make transferability worthwhile. For instance, you may be able to do the transaction without insurance, relying solely on indemnification, if you're working with a reputable seller with a large balance sheet. New technology platforms like Ever.green, Basis, Reunion, and Crux can help you identify and broker these high-quality deals.

How to build a climate-aligned tax credit strategy

Tax credit monetization is much simpler than before, but you still need a thoughtful approach to maximize financial and decarbonization benefits. Follow these 6 steps to get started:

1) Assess the opportunity of tax credit transfers. Think through how to best utilize tax credits in your organization. Are you in a position to buy or sell credits? Did you recently build an onsite generation system whose credits you could monetize for extra cash? Or do you want to purchase credits to reduce your tax basis and help finance your decarbonization initiatives?

Also determine what kinds of tax credits make the most sense for your business, as there are different credit amounts for each.

2) Align transferability benefits with your climate strategy. Identify synergies between your transition strategy and the tax credit marketplace to determine what types of credits will have the highest impact on your climate goals. This could mean purchasing clean fuels tax credits if you're a drayage company or renewable energy investment tax credits if you're a consumer goods company. What are the financial and decarbonization implications of each?

3) Engage and communicate with key stakeholders. You may encounter pushback over why tax credits are a smart use of capital or how the savings should be used, so be sure to engage stakeholders across key departments as you develop your strategy. If you experience resistance, demonstrate how transferability is fundamentally an IRR- and ROI-positive activity and clearly articulate the timelines that can maximize transaction IRRs.

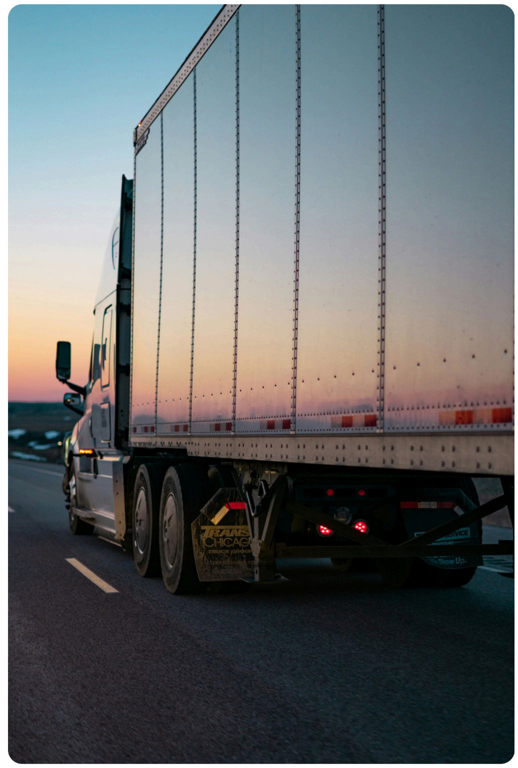
4) Determine how you'll use the tax credit savings. Decide how you'll capture the benefits of your tax credit transaction, whether that's adding the savings to your balance sheet, seeding a green revolving fund, or financing utility-scale clean energy projects to further your climate transition.

5) Identify external support needs. Familiarize yourself with your internal capabilities and identify gaps in support needed to facilitate the transaction. Identify the legal guidance, insurance, and due diligence services required to support the transaction.

6) Vet potential projects. Good projects can be hard to find. Work with the right partner to help you identify and screen potential projects based on your business priorities, decarbonization goals, and stakeholder needs. Which projects can help close your climate finance gap while driving progress toward your emissions reduction targets? Have you identified any social or environmental externalities? How might local communities benefit?

As mentioned above, tax credit transfers aren't without risk. But when structured the right way, they can offer financial and sustainability benefits not found in many other financing mechanisms.

Interested in exploring how to drive ROI and accelerate your climate transition initiatives with tax credit transfers? We've helped numerous companies (buyers) and project developers (sellers) make the most out of tax credits and other IRA incentives. Get in touch with us here.



Earth Finance helps organizations build, finance, and operationalize climate transition strategies, accelerating progress toward a lower-carbon, regenerative economy. We work at the intersection of strategy, policy, finance, and science to help our clients unlock the greatest economic transition in history.

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