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Advancing Health in America

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August 10, 2023

Vivian Hayes
Internal Revenue Service
U.S. Department of Treasury
Room 5203, P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

CC:PA:LPD:PR (REG–101607–23)
Also filed through regulations.gov, IRS and REG–101607–23

RE: Comments on IRS NPRM REG–101607–23 Section 6417 Elective Payments of Applicable Credits under Inflation Reduction Act

IRS-2023-0029-0001

Dear Ms. Hayes,

On behalf of our nearly 5,000 member hospitals, health systems and other health care organizations, our clinical partners — including more than 270,000 affiliated physicians, 2 million nurses and other caregivers — and the 43,000 health care leaders who belong to our professional membership groups, the American Hospital Association (AHA) appreciates the opportunity to submit comments on this important rulemaking to implement the clean energy and energy efficiency incentives in the Inflation Reduction Act of 2022 (IRA). The AHA generally supports the proposed and temporary regulations concerning the election under Section 6417, which was added by the Inflation Reduction Act of 2022 (IRA) and permits certain taxpayers to elect a direct cash payment in lieu of credits.[1] We believe these regulations can be improved in modest ways to make them of greater use to our members and similar organizations for the benefit of the environment.

America's hospitals are working to become more sustainable. Prior to the IRA, however, there were limited opportunities for tax-exempt and governmental hospitals and healthcare providers to take advantage of the tax incentives available to developers of

[1] "Section" references are to the Internal Revenue Code of 1986, as amended (Code), unless otherwise indicated.

and investors in clean energy projects (e.g., depreciation deductions and tax credits). The IRA, through the transferability provisions under Section 6418 and, in particular, the elective direct pay provisions of Section 6417, has provided new opportunities for the healthcare sector to engage in these important clean energy initiatives.

The AHA and other tax-exempt and governmental entities that are generally unable to benefit from tax deductions and credits are supportive of the provisions and policies behind the direct pay provisions of Section 6417 and the proposed regulations promulgated thereunder. At the same time, AHA believes that with certain modifications the elective direct pay provisions of Section 6417 can have an even greater impact and foster rapid adoption among the AHA members of many of the clean energy initiatives set forth in the IRA. We urge you to consider these proposed modifications as you finalize this rule.

Background

The elective direct pay provisions of Section 6417 provide that an “applicable entity” (as defined below) can elect to have the value of the applicable tax credit paid to them directly by the IRS, even if the taxpayer electing direct pay does not otherwise have sufficient federal tax liability to be offset by such credits. Congress intended for the elective direct pay provisions to help certain tax-exempt and governmental entities (including many such entities that are members of the AHA) directly monetize these tax credits. While tax-exempt entities and governmental entities that meet the definition of “applicable entity” may be eligible to elect direct pay for each type of tax credit that has been made available pursuant to the IRA, for-profit companies and other entities (that do not meet the definition of “applicable entity”), can only use direct pay in a limited fashion for (i) the carbon sequestration credit under Section 45Q, (ii) the hydrogen production credit under Section 45V, and (iii) the advanced manufacturing production credit under Section 45X. The IRA defines an “applicable entity” to include (i) any organization that qualifies for exemption from income taxation under the Code, (ii) any U.S. state or political subdivision thereof, (iii) the Tennessee Valley Authority, (iv) certain Indian tribal governments, (v) any Alaska Native Corporation, and (vi) certain rural electric energy cooperatives. Any taxpayer that is not an applicable entity can still benefit from the elective direct pay provisions but only with respect to the three credits referred to above. The proposed regulations refer to such taxpayer as an “electing taxpayer.”

Limitation on Chaining Structures for Tax-exempt and Governmental Entities

The proposed regulations state that any credits for which an election is made under Section 6417(a) must have been determined with respect to the applicable entity or electing taxpayer. This rule requires that the applicable entity or electing taxpayer must own the underlying project or property giving rise to the applicable credit, or, for credits where ownership is not required, the applicable entity or electing taxpayer must otherwise conduct the activities giving rise to the underlying applicable credit. In other words, this rule would prevent an applicable entity from electing direct pay with respect to tax credits acquired from another taxpayer pursuant to the Section 6418 transferability rules (*i.e.*, chaining). This rule, especially when taken in conjunction with the limitation on elective direct pay for partnerships, curtails the ability of tax-exempt entities that would otherwise be applicable entities from participating and investing in clean energy initiatives. For example, a tax-exempt investor seeking to invest in clean energy initiatives would be at a significant disadvantage to its taxable investor counterpart, in that the tax-exempt investor must *directly own* the underlying property (or directly conduct the applicable activities) as opposed to being able to participate in the IRA's greenhouse gas reduction goals by either purchasing tax credits from a transferor under Section 6418 or investing in a partnership that itself will invest in clean energy initiatives and projects.

In addition, the anti-chaining limitation would eliminate the ability of applicable entities to make a direct pay election with respect to credits received under Section 45Q(f)(3) (dealing with transfers of carbon sequestration credits) and with respect to investment tax credits passed through by lessors to lessees using Section 50(d)(4)/Section 48(d) lease pass-through structures. This is a significant limitation in that it eliminates the ability of tax-exempt and governmental entities to take advantage of direct pay through inverted lease structures. For example, if tax-exempt investors could take advantage of direct pay through inverted lease structures, a solar rooftop company could install solar equipment on a hospital's roof, lease the equipment to the hospital, and even though the hospital is not the owner of the equipment, the solar rooftop company would otherwise be able to elect to pass the tax credit along to the hospital. Also, but for the above-described limitation, the hospital/lessee would be able to elect direct pay on the credits passed along from the solar rooftop company/lessor. We believe that permitting this type of structure would incentivize hospitals and other tax-exempt entities to invest in clean energy transitions and investments more rapidly. Moreover, the application of these limitations can be even broader in that the prohibition against chaining structures set forth in the proposed regulations applies not just to (i) credits transferred under Section 6418, (ii) transferred carbon sequestration credits, and (iii) pass-through credits in inverted lease structures, but also applies to any applicable credit "otherwise not determined with respect to the applicable entity or electing taxpayer."

Based on the policy goals of incentivizing broad and rapid adoption of clean energy initiatives by tax-exempt entities and other governmental entities, we respectfully request that the anti-chaining rules be eliminated, as such rules could slow down adoption of clean energy initiatives and delay the ability to achieve the reduced and eliminated greenhouse gas emission targets per the Biden administration's clean energy mandate pledge. Alternatively, we would request that such anti-chaining rules be limited to potentially abusive situations where a principal purpose of the structure is to avoid the transferability rules or otherwise allow taxpayers that are not applicable entities to access the broader elective direct pay provisions.

Limitation on Elective Direct Pay for Pass-through Structures

The proposed regulations provide a broad prohibition on elective direct pay for partnership structures. Specifically, in the case of a partnership or an S corporation, the partnership or S corporation itself (and not the partners of the partnership or the shareholders of the S corporation) must make a direct pay election. The proposed regulations, however, provide that a partnership or S corporation <u>cannot</u> be an applicable entity, and therefore, can only qualify as an electing taxpayer. Based on this limitation in the proposed regulations, a partnership can only elect direct pay for the tax credits available pursuant to Sections 45Q, 45V and 45X, even if the partnership has significant tax-exempt partners that would otherwise be “applicable entities” eligible to elect direct pay for the full set of IRA related tax credits. There was at least some expectation by the AHA and other tax-exempt entities, as well as other commenters, that the regulations would adopt an aggregate approach to the direct pay election to better facilitate the participation of tax-exempt and governmental entities in common industry partnership structures (such as partnership flip structures). The concern is that the co-ownership alternatives proposed by the IRS, including the ability to elect out of Subchapter K or to own property as tenants in common, have numerous requirements and complexities that may otherwise make these provisions of limited applicability for tax-exempt and governmental entities that often must partner with for-profit investors in order to make these investments feasible.

In addition, under the “tax-exempt use property” rules, when a partnership holding tax credit generating property has both taxable and tax-exempt partners, the otherwise available tax credits with respect to the underlying property may be reduced in proportion to the partnership’s tax-exempt partners. Combined, these rules can result in (i) a reduction in otherwise available tax credits to the extent of the partnership’s tax-exempt partners and (ii) an inability to elect direct pay with respect to the portion of the generated tax credits allocable to tax-exempt partners that would have been eligible for the direct pay election if the underlying property were held directly by the tax-exempt partners.

Based on the above, we believe that it would be beneficial from a policy perspective to apply an aggregate approach to the elective direct pay rules under Section 6417 that would either (i) permit a partnership to make a direct pay election with respect to the portion of the underlying credits that would otherwise be allocable to qualified partners in such partnership (i.e., partners that would themselves be applicable entities) or (ii) permit applicable entities that are partners in a partnership to elect direct pay notwithstanding that, under both alternatives, the for-profit partners of such partnership are limited to either receiving credit allocations or the credit transferability rules of Section 6418. This approach would greatly and rapidly encourage a broader adoption of clean energy initiatives among applicable entities that frequently partner with for-profit investors to achieve these goals. The direct pay benefit would still be beneficially limited to persons that would otherwise qualify as applicable entities, such that partners of a partnership that do not otherwise qualify as applicable entities would still only be able to benefit from the direct pay provisions to the extent they are electing taxpayers and only with respect to the tax credits pursuant to Sections 45Q, 45V and 45X.

For example, assume Partnership ABC has three partners — a tax equity investor (“Partner A”), a developer (“Partner B”), and a tax-exempt investor (“Partner C”). Partnership ABC invests in a solar facility seeking to claim an investment tax credit (ITC) on $100 of eligible basis, which assuming a 30% ITC would generate $30 of tax credits. The surprising result of these rules would seem to be that (i) the participation of Partner C could limit Partnership ABC’s ability to claim the full $30 tax credit, which (assuming Partner C is investing directly and not through a blocker corporation) could be significantly reduced under the “tax-exempt use property” rules and (ii) notwithstanding the ITC haircut attributable to Partner C being a partner in Partnership ABC, because the partnership is not an applicable entity and because Partner C does not directly hold the tax credit producing property, neither Partnership ABC nor Partner C would be able to elect direct pay to be made whole for the reduced tax credit. This result does not seem to be in accordance with the policy underlining the IRA and the elective direct pay rules.

We appreciate your consideration of these issues. Please contact me or Chad Golder, AHA’s deputy general counsel, at cgolder@aha.org, if you have questions.

Sincerely,

/s/

Melinda Reid Hatton
General Counsel and Secretary