

Tribal Community Solar Federal Tax Incentives

“Direct Pay” Explained

What is direct pay? How does it impact the economic viability of Tribal community solar projects?

The 2022 Inflation Reduction Act (IRA) opened the doors for tax-exempt entities to receive a cash payment for solar panel installations through a program called “direct pay” or “elective pay.”

Prior to 2022, Tribal Nations typically did not have access to tax incentives due to their status as tax-exempt entities. This meant that Tribal-owned solar projects were functionally more expensive than solar projects owned by non-Tribal entities that could take advantage of the federal Investment Tax Credit (ITC) and a reduction in income taxes. To claim renewable energy tax credits and reduce the project’s capital costs, Tribes were required to structure deals with a tax equity partner.

Now, through direct pay, Tribes can receive a cash payment for the amount of the tax credit’s value for installing a solar facility. Through the IRA, the federal government will return to tax-exempt entities 30 to 70 percent of the costs for qualifying renewable energy systems, including Tribal community solar projects. Tribal Nations and tax-exempt entities will be paid in tax refunds, instead of reducing their owed taxes.

If your Tribe has any questions about direct pay tax incentives, please contact us.

info@sovereignenergy.org

Incentives

The base incentive for qualified tax-exempt organizations is 30 percent of the installation cost.

Additional Incentives

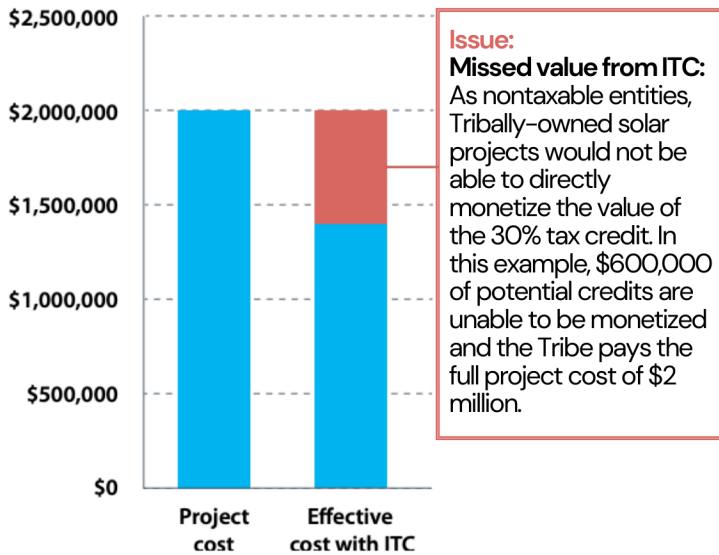
- 10% energy community bonus if the project is located on a brownfield site, in a fossil fuel community with high unemployment, or in a former coal community. Some, but not all Tribes in New Mexico, qualify as “energy communities” by the U.S. Department of Energy.
- 10% domestic content bonus if all the steel and iron products and a set percentage of the manufactured products used in the project were made in the United States.
- 10% low-income community bonus if the project is sited in a low-income community, on Tribal land, or for affordable housing development.
 - 200MW of allocation is reserved for projects on Tribal lands with preference given to projects owned by a Tribal enterprise
 - Distributed energy systems for low-income residential buildings can claim an additional 20 percentage points (instead of the 10 percent point bonus) if the system provides enough energy for at least 50 percent of the building’s energy needs

How does direct pay work with other project funding sources?

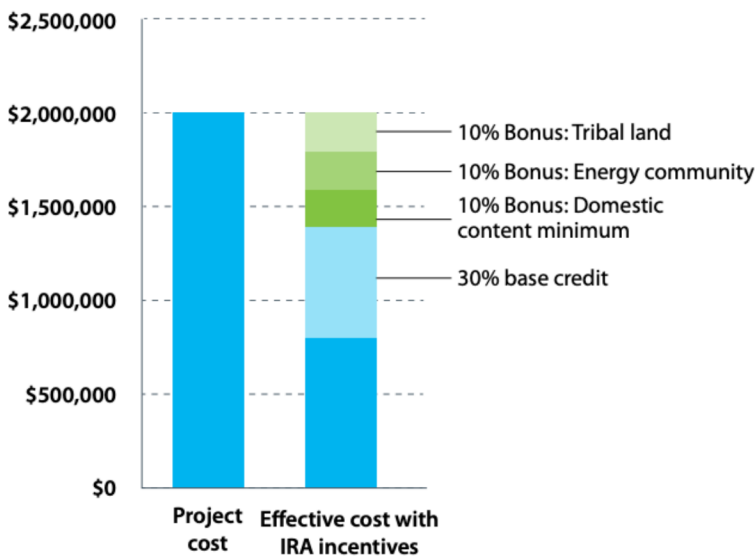
Direct pay and federal or state grant funding **can** be used on the same community solar project. However, in some instances, the amount of the tax credit and direct payment must be reduced if nontaxable grants or other nontaxable proceeds are used.

Tribal Solar Projects

Example: 1-MW Tribal Solar Project **Before IRA Provisions**



Example: 1-MW Tribal Solar Project **After IRA Provisions**



IRA benefits:

New mechanisms for Tribes to receive the value of the ITC: The IRA allows Tribes to monetize the value of the ITC through the direct pay option and transferability of credits. In this example, the combined value of the ITC is \$1.2 million, which reduces the effective cost of the project to \$800,000.

Potentially larger ITC credits: Tribally owned solar projects that meet certain criteria have the potential to receive larger credits than in the past. This example shows that the new IRA incentives could double the ITC credit to 60% for a project that received the base ITC rate combined with the domestic content bonus, energy community bonus, and Tribal Land bonus.

Source: NREL: [Addressing Regulatory Challenges to Tribal Solar Deployment](#)

How do I apply for direct pay?

Note: Due to the complexities of these projects, it is recommended to hire a tax attorney to assist with this process.

Step 1: Identify the project and the credit you want to pursue.

Step 2: Complete your project, place it into service, and determine the corresponding tax year.

Step 3: Complete pre-filing registration with the IRS before your tax return is due.

Note: Receiving the registration number in the pre-filing registration process is not a determination that a Tribe qualifies for the credit or for direct payment. The IRS can still perform a tax audit.

Step 4: Request direct pay using an annual tax return and receive direct payment from the IRS.

How long will direct pay be available?

The tax credits last at full value through at least 2033. The IRS will be accepting application submissions on a rolling basis.

How Does The Direct Pay Option Work?

The incentive is only earned the year the project is turned on (and only paid by the IRS the following year, when the organization's tax return is submitted and processed).