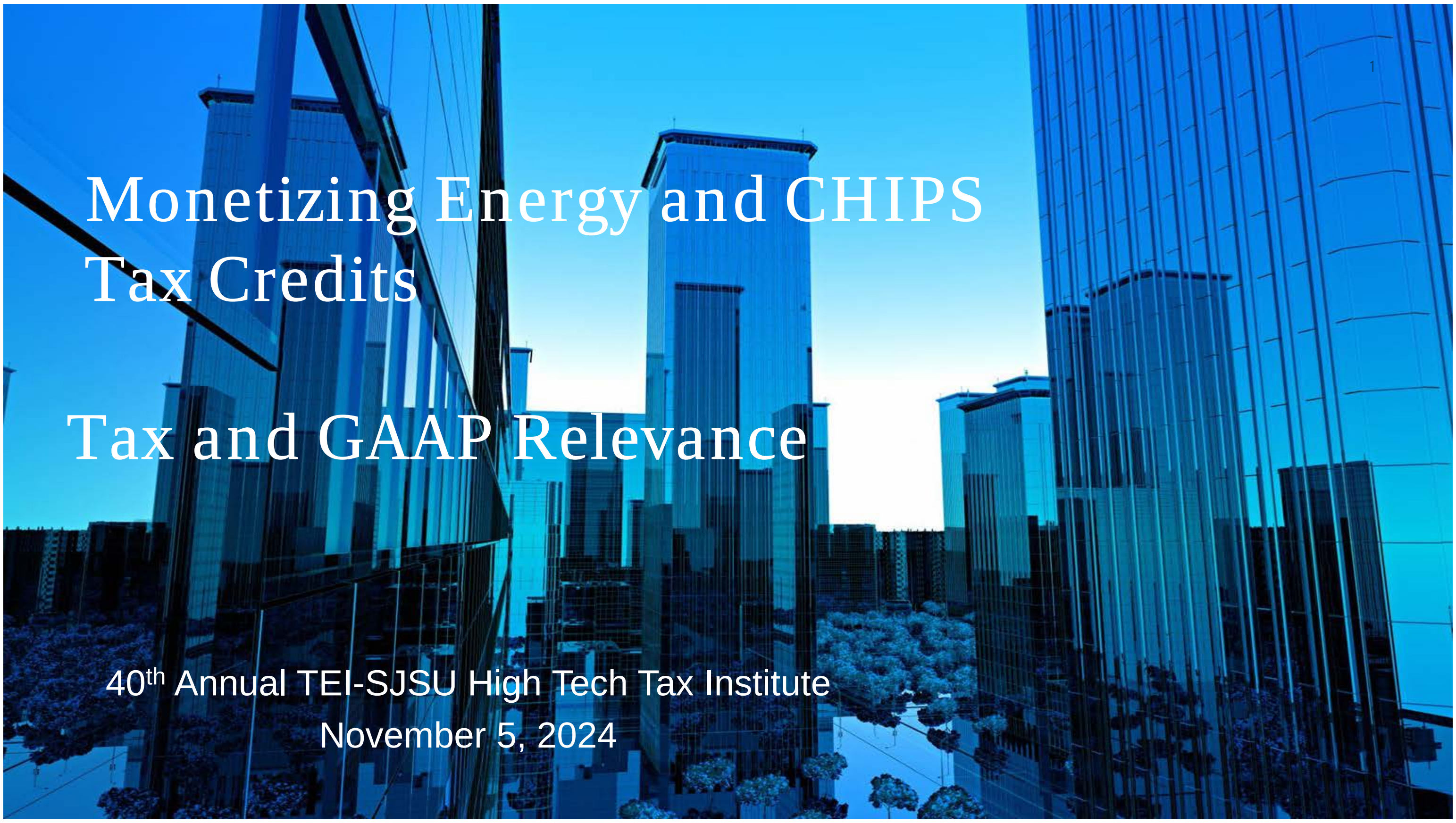

Agenda

- Introductions
- Setting the Stage
- Monetization – What are the rules? How would the process work?
- Market Trends
- Value Erosion – SALT, CAMT, Pillar 2 & BEAT Considerations
- GAAP Implications
- Key Takeaways
- Questions?

Today's Presenters

Wendy Punches
Managing Director
PwC

Jared Huish
Partner
KPMG

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Principal
BDO

Brent Sabot
Manager
RSM

Setting the Stage

CHIPS ACT

- Historic bipartisan investment to:
  - Spur American-made semiconductors,
  - Tackle supply chain vulnerabilities by making more goods in America
  - Revitalize America's scientific research and technological leadership
  - Strengthen economic and national security
- Includes Grants and a Tax Credit
- Investment Tax Credit
  - 25% of an eligible taxpayers qualified investment in an advanced manufacturing facility
  - Equipment and Building Structures Eligible
  - "Direct Pay" option

Inflation Reduction Act

- Signed into law on August 16, 2022
- Largest federal investment in clean energy in US history; reinstates and significantly expands current incentives providing an estimated range $780 billion - $1.2 trillion* of new energy related tax credits over 10 years
- Aims to advance the economy by promoting growth in targeted areas
- In addition to significant energy provisions, the bill also aims to advance the economy further into social policy by creating a tiered credit structure
- Many of the credits require LCAs, and beginning in 2025 go to a technology neutral credit.
- Additional monetization opportunities
  - Direct Pay
  - Transferability

Setting the Stage

Code sections enacted or significantly amended by IRA		No or conforming amendment
25C energy efficient homes 25D residential clean energy 25E used clean vehicles **(new)** 30C alternative fuel vehicle refueling property 30D clean vehicles 40 alcohol, etc. used as fuel 40A biodiesel /renewable diesel 40B sustainable aviation fuel **(new)** 45 clean electricity production 45J clean nuclear power production 45Q carbon oxide sequestration	45U zero-emission nuclear power plant production **(new)** 45V clean hydrogen production **(new)** 45W commercial clean vehicles **(new)** 45X advanced manufacturing production **(new)** 45Y clean electricity production **(new)** 45Z clean fuel production **(new)** 48 energy property 48C qualifying advanced energy project 48E clean energy investment **(new)** 179D energy efficient commercial buildings deduction	30B alternative motor vehicles 43 enhanced oil recovery 45H low sulfur diesel fuel production 45I oil and gas from marginal wells 45K fuel from nonconventional source 45L new energy efficient homes 48A qualifying advanced coal project 48B qualifying gasification project

Setting the Stage

Credit bonuses

- Prevailing wage and apprenticeship (PWA)
- Domestic content
- Energy community
- Low-income community

	ITC (Section 48/48E)	PTC (Section 45/45Y)
Base	6%	0.3 cents *
With PWA	30%	1.5 cents *
Domestic content	+2% (without PWA) or 10% (with PWA)	+10%
Energy community	+2% (without PWA) or 10% (with PWA)	+10%
Low-income community	+10% or 20%	NA

* Adjusted annually for inflation

Credit Monetization

The rules

Monetization - Direct Pay vs Transferability

Direct Pay (Sec. 6417):

- Taxpayers that fall within the definition of ‘applicable entities’ (i.e., tax-exempt entities, state & local governments, etc.) can elect to be treated as having made a payment of tax equal to the value of the credit they were eligible for
- 12 IRA credits + 48D
- The limitation on applicable entities does NOT apply to credits for:
  - Carbon capture and sequestration (Sec. 45Q)
  - Clean hydrogen (Sec. 45V)
  - Advanced manufacturing production credit (Sec. 45X)
- Election made at the entity level, not the partner or shareholder level

Transferability (Sec. 6418):

- Generally, entities that are not applicable entities under the direct pay rules may transfer certain tax credits to third parties (must be sold for cash)
- Transfer may be for a portion or all of a credit
- No re-transfers allowed, and no deduction for buyer or income inclusion for seller
- Election made at the entity level, not the partner or shareholder level

Significant Market Activity!

Direct Payments

12 Applicable IRA credits:

- Alternative Fuel Vehicle Refueling Property – §30C
- Zero Emission Nuclear Power Production – §45U
- Advanced Manufacturing Production – §45X
- Energy Property Investment – §48
- Renewable Electricity Production – §45
- New Clean Hydrogen PTC – §45V
- Clean Electricity Production – §45Y
- Extension of Advanced Energy Project – §48C
- Carbon Capture & Sequestration – §45Q
- Qualified Commercial Clean Vehicles – §45W
- Clean Fuel Production – §45Z
- Clean Electricity Investment Tax – §48E

Monetization - Direct Pay - Overview

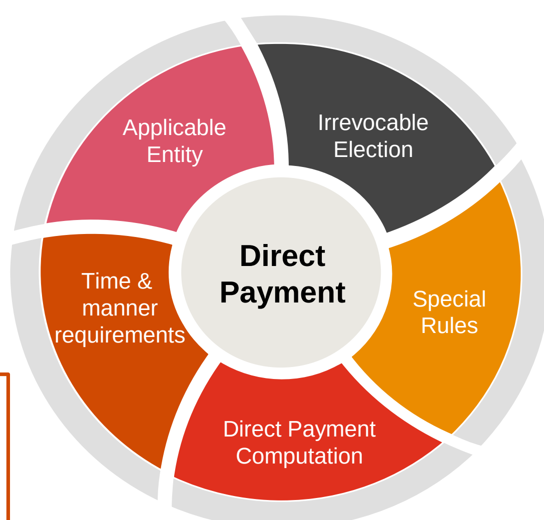
Direct Pay ("Elective Payments") – Final Regulations

Applicable entity generally is tax-exempt entity (including government, TVA, Indian tribal governments, and Alaska Native Corporations)

- Other taxpayers may elect direct payment for credits under Sections 45Q, 45V, and 45X
- Elected on property-by-property or facility basis and for full amount of credit

Pre-filing registration through IRS electronic portal required

- Election made by original tax return no later than extended due date



Election generally irrevocable; for some taxpayers and some credits, applies for a period of years (5, 10, or 12)

Special rules for partnerships and S corporations

Direct payment exceeding allowable credit is subject to tax plus 20% of excess

Elective payment

- The "net elective payment amount" treated as payment against tax
  - Is lesser of
    - (1) aggregate of all applicable credits **or**
    - (2) the total GBC (including applicable credits) over the total GBC allowed against tax liability (determined without regard to Section 38(c), GBC limitation rules)
  - Credit amount reduced to zero for purposes of GBC
  - Removes direct payments from GNC credit limitation but includes direct payments in GBC if necessary to lower tax liability to the GBC limitation
  - Payment is treated as made on the later of unextended return due date or return filing date

Hypothetical #1		
Tax Liability		1,333
Allowable GBC *		1,000
GBCs		
R&D		600
45X		1,400
Total GBC		2,000
NEP - **lesser of**		
Aggregate of applicable credits		1,400
	OR	
Total GBC over total allowed		1,000
Net elective payment amount		1,000
So net elective payment amount		1,000
R&D		600
45X		400
		2,000

Hypothetical #2		
Tax Liability		1,333
Allowable GBC *		1,000
GBCs		
R&D		2,000
45X		1,500
Total GBC		3,500
NEP - lesser of		
Aggregate of applicable credits		1,500
	OR	
Total GBC over total allowed		2,500
Net Elective payment amount		1,500
So net elective payment amount		1,500
R&D		1,000
Carryforward of R&D Credit		1,000
		3,500

Hypothetical #3		
Tax Liability		1,333
Allowable GBC *		1,000
GBCs		
R&D		-
45X		3,500
Total GBC		3,500
NEP - **lesser of**		
Aggregate of applicable credits		3,500
	OR	
Total GBC over total allowed		2,500
Net Elective payment amount		2,500
So net elective payment amount		2,500
45X as a credit		1,000
		3,500

* Assumes there are no credit carryforwards

Energy Credit Transfers

- For tax years beginning after 2022, taxpayers may elect to transfer all or a portion of an eligible credit to an unrelated party
- Not available for applicable entities
- Not available for Section 48D credit, progress expenditures or general business credit carrybacks or carryforwards
- Eligible taxpayer must own the underlying property or, if ownership is not required, conduct the activities giving rise to the credit
- Unrelated party - Reference 267(b) or 707(b)(1) 50% relatedness threshold

Eligible Credits

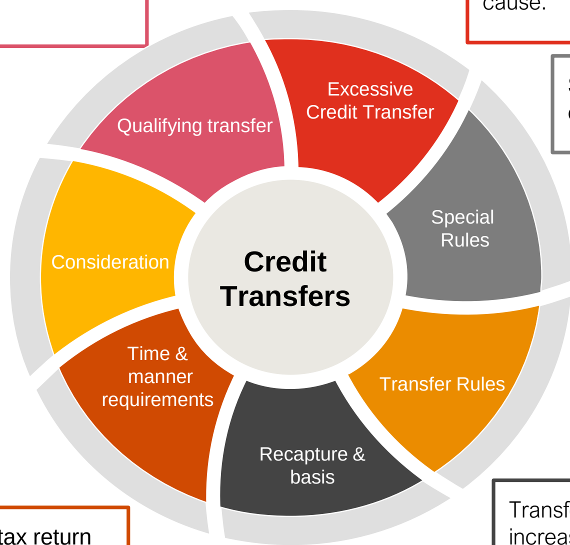
- Alternative Fuel Vehicle Refueling Property – §30C
- Zero Emission Nuclear Power Production – §45U
- Energy Property Investment – §48
- Clean Electricity Investment Tax – §48E
- Renewable Electricity Production – §45
- New Clean Hydrogen PTC – §45V
- Clean Electricity Production – §45Y
- Extension of Advanced Energy Project – §48C
- Carbon Capture & Sequestration – §45Q
- Advanced Manufacturing Production – §45X
- Clean Fuel Production – §45Z

Monetization – Transferability - Overview

- Not available for tax-exempt entities or Section 48D credit, progress expenditures or general business credit carrybacks or carryforwards
- 11 credits are eligible

Transferee taxpayer is subject to tax on the excess of the credit transferred over the allowable credit plus 20% of the excess, unless demonstrates reasonable cause.

- Consideration must be paid in cash to an unrelated party
- Consideration is not taxable income to the transferor and not deductible by the transferee
- Transferee does not realize gross income if the amount paid is less than the amount of the credit transferred
- Can only be transferred once
- 3 year carryback, 22 year carryforwrd



Special rules for partnerships and S corporations

- May transfer part of a credit and portions of single credit to different transferees
- Transferee may not further transfer the credit
- Transferee of the credit is treated as the taxpayer regarding the credit for all income tax purposes
- Transferee can use for ETP credits it has purchased, or intends to purchase

- Election made on original tax return no later than extended due date
- Pre-filing is required

Transferee taxpayer responsible for the increased tax and the eligible taxpayer increases the basis of the investment credit property.

Monetization – Significance

Pre-IRA Project Financing

- Due to their lack of sufficient tax capacity, developers of renewable energy projects generally had to rely on complex tax equity structuring to monetize associated federal tax credits. A tax equity investor is an equity owner of the project taking on project risks with significant upfront resources related to legal, structuring, HLBV/PAM accounting, and tax K-1s.
- Tax equity investments were structured through: Partnership Flips / Sale-Leasebacks / Inverted Leases

Post-IRA Project Financing

- Simplifies project structuring through two new monetization options: direct pay and **credit transferability.**
- In a transfer, a tax credit is transferred via a Purchase and Sale Agreement.
- Minimal accounting complexity
- Limited risks such as operational/project risks as the corporate buyer of tax credits is only purchasing the rights to the tax credit(s) and is not considered an owner of the assets
- Simplified tax reporting as ownership of the project no longer required
- Cash tax savings, free cash flow, and US GAAP effective tax rate benefit

Credit Monetization: General Process To Execute a Transfer

– PHASE 1: Tax Modeling – Quantifying tax appetite

– PHASE 2A: Engage legal counsel representation

– PHASE 2B: Define timing and credit type considerations

– PHASE 3: Source credits

– PHASE 4: Letter of Intent / Due Diligence

– PHASE 5: Negotiate and execute the PSA

Credit Monetization: General Process To Execute a Transfer

PHASE 1 Tax Modeling – Quantifying Tax Appetite	▶ Understand the organization's tax appetite based upon forecasted tax positions. Federal transferable credits are treated as General Business Credits (GBC). ▶ Tax limitations or other attributes may exist that limit the overall tax appetite such as Foreign Tax Credits, OECD Pillar Two, other GBCs (e.g., R&D), and the overall GBC limitation. ▶ Tax modeling may focus on the current year only or consider the expanded 3-year carryback window.
PHASE 2 Define Timing and Credit Type Considerations	▶ Align the organization's cash flow availability for purchase of federal transferable credits. Cash set aside for tax estimates may be reallocated. ▶ Based upon tax appetite and cash flow needs, determine strategy on a quarterly versus annual purchase of credits. ▶ Transferable tax credits represent either Production Tax Credits (PTC) or Investment Tax Credits (ITC).
PHASE 3 Source Credits	▶ Identify available credits based upon earlier tax appetite parameters determined in Phase 1 & 2. Credits may also be sourced by credit type, technology, location, or risk management (i.e., seller provided indemnification or tax credit insurance). ▶ Prior to project summary reports being shared for management review/consideration, Non-Disclosure Agreements are executed.
PHASE 4 Letter of Intent/ Due Diligence	▶ Pending management review, a Letter of Intent is provided to the seller of available credits expressing formal interest. ▶ Upon acceptance by seller, diligence performed on the underlying merit of the credit to assess risk (e.g., was the project developed in an appropriate structure to avoid Investment Tax Credit Recapture). ▶ For insured credits, discretion may be considered on the level of diligence as insurance providers perform their own diligence for underwriting purposes.
PHASE 5 Negotiate and Execute PSA	▶ Credit transfer agreement negotiated and reviewed with an organization's preferred counsel. ▶ Purchased credits become available to offset an organization's applicable tax liability ▶ Seller provides buyer with a copy of the transfer election statement included on buyer's tax return along with underlying documentation required to report the credit transfer to the IRS. ▶ Pay for tax credits (upon execution and/or through agreed upon installment payments).

Credit Monetization: Risks and Mitigation

Risk Category	Documents for Due Diligence/Risk Mitigation
Qualification – *Does the project or activity qualify for the credit and any applicable bonus credits/adders?*	-Utility permission to operate letter or equivalent -Independent engineer reports -Documentation of begun construction -If not safe harbored, adherence to PW&A requirements (e.g., certified labor payroll, apprentices hour logs, etc.) -Documentation substantiating eligibility for bonus credits (e.g., location of project for energy community, supplier cost data and steel/iron certifications for domestic content)
Quantification – *For ITCs, was the project cost basis properly calculated, and were only eligible expenses included? For PTCs, was the correct rates utilized and is production verifiable?*	-Third-party cost certification for ITCs -Audited financials -Operating reports
Recapture* - *Was the project abandoned, foreclosed, or sold within five years of the placed in service date?* **Risk category specific to Section 48 ITCs and not applicable to Section 45 PTCs.*	Documentation on credit worthy off-taker for entire recapture period, structure of debt, sufficient property/causaly insurance, and site control
Counterparty Risk – *If losses are realized, can buyer collect damamages against seller/credit worthy entity?*	-Financials of sellers and any guarantor -Tax credit insurance

Tax Credit Transferability Term Sheet Assistance and Due Diligence

Term Sheet	Buy Side Due Diligence	Sell Side Due Diligence
Cost of Capital Matters	**Credit Eligibility and Rate Considerations**	**Credit Eligibility and Rate Considerations**
• Year-end considerations • Timing of payments • Estimated tax off-sets	• Assessment of technological criteria • Base Rate • Special considerations for each credit	• Credit computation support • Cost Segregation • Special considerations for each credit
Key Terms not to Sleep On	**Assess Technical Considerations**	**Technical Considerations**
• Who is providing the indemnification? • What does insurance cover? • Who gets to control the audit?	• Begun Construction considerations • Placed in Service assessment • Tax ownership review • Eligible basis review • Eligibility of Transferor • Assess Transferor's documentation procedures • "Cash" considerations	• Begun Construction analysis/documentation • Placed in Service assessment/documentation • Tax ownership analysis • Eligibility of Transferor • Review partnership agreements • "Cash" considerations
There is no "Market" Yet	**Assess Risk Profile**	**Reduce Risk Profile**
• Assume all terms are negotiable • The last deal is not yet real precedent • Our clients are the whales here – help them act like it	• "Excessive Credit" Transfer mitigation • Passive Activity Rule implications • At Risk rule implications • Recapture risk mitigation • Evaluation of supporting documentation	• "Excessive Credit" Transfer mitigation • Passive Activity Rule implications • At risk rule implications • Recapture risk mitigation • Assist with documentation policies/procedures

Credit Monetization: Pricing Trends

	Description	Risk mitigation	Pricing*
Current-year PTCs	Proven technologies such as wind or solar	Seller indemnity is typically provided. PTCs do not carry recapture risk.	**$0.95** Multi-year or forward PTCs will trade at a discount
De-risked ITCs	Proven technology such as solar or battery storage. Typically above $10M in volume; larger projects trade at a smaller discount	Assumes insurance and/or indemnity from a credit-worthy guarantor	**$0.93**
More complex ITCs	Technologies with lower buyer demand such as biogas, or smaller transactions (<$10M) with any technology	Assumes insurance and/or indemnity from a credit-worthy guarantor	**Low $0.90s**
Small Credits / Uninsured ITCs	New technologies. Projects without insurance (e.g. smaller projects <$5M or smaller developers)	No insurance. Indemnity from a credit-worthy guarantor	**Varies by situation ($0.80s)**

**Reflects final pricing to credit buyer. Pricing is subject to change based on market conditions and specific project facts and circumstances*

Credit Monetization: Tax Credit Market Forecast

Demand for Tax Credit Buyers:

The IRA will incentivize an increase in clean energy investments in the U.S., resulting in an increased demand for investors that can absorb the tax credits generated from these activities.

Transferability expands the group of potential purchasers to include non-traditional tax equity investors, enabling any U.S. corporate taxpayer to buy these credits at a discount and assist in financing domestic clean energy projects.

Figure 5: US ITC and PTC require ~US$500 bn of tax equity to monetize ITC/PTC and depreciation benefits

Source: Credit Suisse 2022 ESG Report – Treeprint US Inflation Reduction Act

Value Erosion - SALT, CAMT, Pillar 2 & BEAT Considerations

State & Local Tax Considerations

- For federal purposes – No income to the seller, no deduction for the buyer
- Credit purchaser does not recognize gain on the use of credits for federal income tax purpose
- Tax treatment for state purposes may vary
- Consider modeling state tax costs and consult with a state tax expert

Corporate Alternative Minimum Tax (CAMT) Considerations

- Credit buyers can use purchased IRA credits to offset the CAMT tax

Base Erosion and Anti-Abuse Tax (BEAT)

- BEAT imposes adverse treatment on some tax credits, including PTCs & ITCs
- Only 80% of the value of renewable energy tax credits may be used against the BEAT tax in each year through 2025. After 2025, none of the renewable energy tax credits may be used against a taxpayer’s BEAT tax liability

Pillar 2 Considerations

- For the buyer, the IRA credits are considered non-marketable credits. For non-marketable credits, the numerator of the ETR ratio is only reduced by the discount on the credit
- Staggered implementation of the pillar 2 rules across jurisdictions poses a risk that benefit of credits may be clawed back under pillar 2

How are different credits treated for Pillar 2?

Qualified Refundable Tax Credits (“QRTCs”)	Non-QRTCs	Market Transferable Tax Credits (“MTTCs”)	Non-MTTCs	Other Tax Credits (“OTC)
• Refundable (paid cash / cash equivalents) within 4 years of CE being eligible for credit • Face value of credit generally **treated as GloBE Income** in the year entitlement accrues • May be recognized as deferred income over useful life of assets consistent with accounting treatment	• Refundable (in whole or in part) but do not meet QRTC requirements • **Treated as a reduction to Covered Taxes.**	• Can be used by holder to reduce covered taxes in *issuing jurisdiction AND* • Meets legal and transferability standards in the hands of the holder (based on whether originator or purchaser) • Broadly **treated as GloBE Income**	• Does not meet the MTTC requirements in the hands of the originator and / or the purchaser. • **Treated as reduction to Covered Taxes** to the extent that the non-MTTC is used to satisfy tax liability. Reduction equal to amount of credit less purchase price.	• Not refundable and non-transferable credits that can only be used to offset the covered tax liability of the CE (e.g.: U.S. R&D credit) • **Treated as a reduction to covered taxes.**
Example: UK and Ireland refundable R&D credit **US Sec. 45X**		**Example: US IRA transferable tax credits (seller)**	**Example: US IRA transferable tax credits (buyer)**	**Example: US R&D credit**

Why does it matter?

Tax credits, when treated as a reduction to Covered Taxes (numerator), reduce the Jurisdictional ETR to a greater extent than when treated as an increase to the GloBE Income (denominator).

QRTCs and MTTCs

PTBI:	100
Credit:	10
Post-credit PTBI:	110
Book Tax Expense:	21
After Tax Profit:	89

U.S. Jurisdictional ETR:

GloBE Income = 110
Covered Taxes = 21
ETR = 19%
Top-up tax = 0

Non QRTCs, Other Tax Credits, and Non-MTTTs (to extent of discount)

PTBI:	100
Pre-credit book tax:	21
Credit:	10
Book Tax expense:	11
After Tax Profit:	89

U.S. Jurisdictional ETR:

GloBE Income = 100
Adjusted Covered Taxes = 11
ETR = 11%
Top-up tax = 4

Big picture: U.S. R&D credit is an OTC and thus a reduction to Covered Tax, this can cause low U.S ETRs. There is ongoing discussion of a potential clarification to the Pillar 2 rules that would allow the U.S. R&D credit to be treated as an increase to income.

IRA Transferable Tax Credits

Name of the credit	Refundable / Direct Pay	Transferable
Section 30C Alternative fuel vehicle refueling property credit		X
Sections 45, 45Y Clean electricity production tax credit		X
Section 45Q Credit for carbon oxide sequestration	X	X
Section 45U Zero-emission nuclear power production credit		X
Section 45V Clean hydrogen production tax credit	X	X
Section 45 W Qualified commercial vehicles		
Section 45X Advanced manufacturing production credit	X	X
Section 45Y Clean electricity production tax credit		X
Section 45Z Clean fuel production credit		X
Sections 48, 48E Clean electricity investment tax credit		X
Section 48C Qualifying advanced energy project credit		X

Pillar 2 treatment of transferable credits

- IRA transferable credits are generally expected to be:
  - MTTCs in the hands of the Originator
    - As a result, the credit, or transfer price if actually transferred, is treated as an increase to the Originator's GloBE Income
  - Non-MTTCs in the hands of the Purchaser
    - As a result, the discount (i.e., face value less purchase price) is treated as a reduction to the Purchaser's Covered Taxes
- **Simple example:**
  - Originator sells a $100 IRA Transferable Credit to Purchaser for $95
    - Originator will have a $95 increase to its GloBE Income
    - Purchaser will have a $5 reduction to its Covered Taxes

Big picture: If US ETR was ever to be 15% (or less), the benefit of purchasing IRA credits ($5 of benefit in example above) would be clawed back by the UTPR. Furthermore, the transferable credits rules have NOT been comprehensively incorporated into national legislation so there is risk that the answer is even worse than a $5 reduction to tax expense.

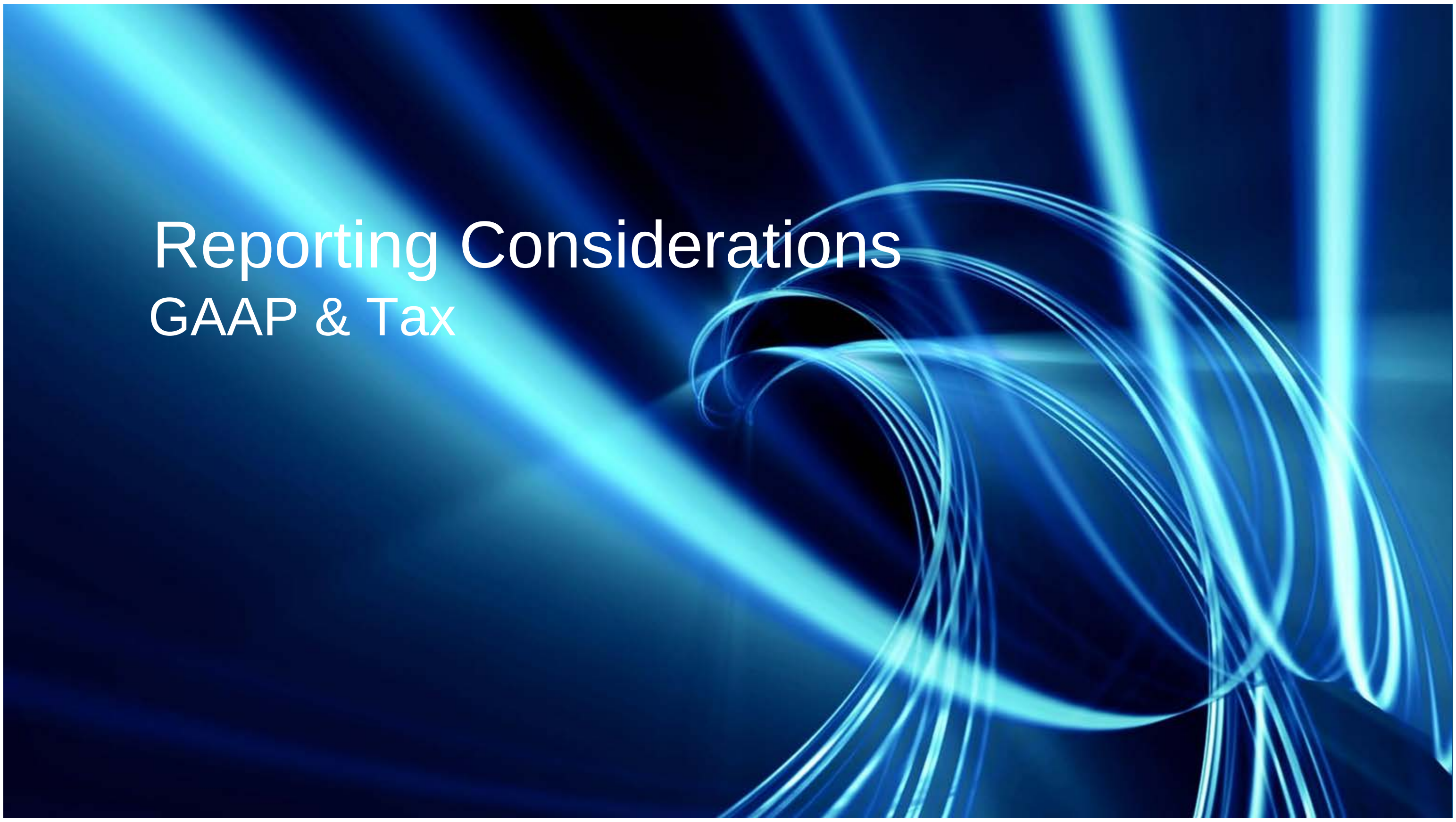
Transferable credit rules not yet formally enacted in several jurisdictions

	Jurisdiction	Enacted legislation includes transferable credit rule?
1	Austria	Yes
2	Belgium	Yes
3	Bulgaria	No
4	Croatia	No
5	Czech Republic	Yes
6	Denmark	Yes
7	Finland	No
8	France	No
9	Germany	Yes
10	Greece	
11	Hungary	Yes
12	Ireland	Yes
13	Italy	Yes
14	Liechtenstein	
15	Lux	No
16	Netherlands	No
17	New Zealand	
18	Romania	No
19	Slovenia	
20	South Korea	Yes
21	Sweden	No
22	Turkey	

As of September 2024

Credit carryforwards – focus on CAMT

- Another important consideration related to tax credits is credit carryforwards (R&D, CAMT, FTC)
- Pillar 2 has a general rule (Article 4.4.1(e)) that the deferred taxes related to tax credits are disregarded
- However, a DTA on a tax credit that exists prior to the Transition Year is regarded on reversal
- For example, if the Company had a CAMT liability in FY25 the DTA related to that liability should be pre-Transition Year for the U.S. (since no Pillar 2 rule applies to the U.S. in that year) and thus the reversal of that DTA in a future year would be regarded mitigating a low U.S. ETR.
  - If the CAMT liability arose after the Transition Year, the DTA would be disregarded (when generated and utilized) potentially leading to low tax income in future years when the credit carry-forward is utilized
  - Simple Example:
    - Assume a Company pays 5 of CAMT in a post Transition Year and books a DTA of 5. In a future year, the Company has 100 book income, 20 of pre-credit current tax, 5 CAMT carryforward, and thus 15 of current tax expense. While there would be 5 of deferred tax expense for book purposes, that deferred tax is disregarded and therefore Pillar 2 Covered Tax equals 15. If the company has even 1 of permanent benefit in that year e.g., R&D credit, it would trigger Pillar 2 top-up tax in that year.



Accounting for tax credits

We believe the accounting for credits generally depends on whether a company can obtain the benefit from the taxing authority only through reduction of its income tax liability.

Nonrefundable		Refundable
Nontransferable credits The benefits of nonrefundable, nontransferable credits are realizable only if the company has a sufficient amount of income tax liability to utilize the credit. Nonrefundable, nontransferable credits are accounted for under ASC 740	**Transferable credits** The transferability feature introduces more complexity in the accounting for the credit when it arises and when it is sold. We believe entities can make an accounting policy election to either apply ASC 740 or account for as government grants	The benefits of refundable credits are not limited by a company's taxable income or tax liability. We believe refundable credits should be accounted for consistent with an entity's policy on government grants

Refundable and transferable credits

Generally, tax credits, other than certain investment tax credits and the below, should be recognized as a reduction of income tax expense in the period they arise. However, there are differing accounting treatments for transferable and refundable credits.

Transferable	We believe it is most appropriate for companies to apply ASC 740 to nonrefundable, transferable credits. • A company may either consider or disregard expected transfers of the credit in assessing the realizability of the credits • If sold, recognize the sale proceeds and derecognize the carrying amount of tax asset (the gain (loss)) as adjustments to income tax expense (benefit) • We also believe it is acceptable for companies to recognize the gain (loss) on sale of the credits in pretax income We believe it is acceptable to account for the credits like government grants
Refundable	Credits not dependent on an entity's tax liability are not considered a part of income taxes and are outside the scope of ASC 740. • The benefit for these credits should be recorded consistent with an entity's policy on accounting for government grants.

Accounting for the purchase of the credit

Buyer may purchase tax credit at discounted price

The difference between the purchase price, including direct costs to acquire the credit, and the ASC 740 measurement is recognized as a deferred credit.

The deferred credit is recognized in income tax expense in proportion to the reversal of the associated deferred tax asset.

Sellers and buyers may incur costs related to purchasing tax credits

Buyer: Legal costs, accounting advice, tax advice, tax compliance, (named beneficiary of seller purchased tax insurance)

Seller: Legal costs, accounting advice, tax advice (often tax opinion), tax compliance, sales commission, (indirect beneficiary of tax insurance if indemnity in place)

Indemnity accounting can create complexity

Presentation

If credit can only be used to offset current or prior year income tax liability, we believe it has an accounting policy choice for presentation of acquired credit:

- Adjustment to income taxes refundable (payable)
- Deferred tax asset

If purchased credit is expected to be carried forward to be utilized on future income tax returns, present as deferred tax asset.

Government grants

- In certain instances, a government provides a taxpayer with a refundable credit.
  - Because the right to receive the benefit from a refundable credit does not depend on the existence of an income tax liability, we believe refundable credits should be accounted for as a government grant.

U.S. GAAP contains no grant accounting guidance that explicitly applies to for-profit companies. In practice, one of the following is applied by analogy to account for these types of credits

IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*	**ASC 958-605**, *Not-for-profit entities – revenue recognition*	**ASC 450-30**, *Gain Contingencies*

Government grants disclosure requirements

ASC 832, *Government Assistance*, requires business entities to make annual disclosures about transactions with a government that are accounted for by applying a grant or contribution accounting model by analogy.

- An entity shall disclose the following about transactions with a government:
  - The nature of the transactions, including a general description of the transactions and the form in which the assistance has been received
  - The accounting policy used to account for the transactions
  - The line items on the balance sheet and income statement affected by the transactions, and the amounts applicable to each financial statement line item in the current reporting period
  - Significant terms and conditions of the assistance (including commitments and contingencies).
- Transactions, including government assistance, that are within the scope of ASC 740 are excluded from the scope of ASC 832.

Simple Example: Reporting Considerations - GAAP

FACTS:
Company purchases a credit of $40,000,000 for $37,200,000 in 2023. The Credit is used in full during 2023.

AT THE TIME OF PURCHASE	
DR Deferred Tax Asset ("B/S")	$40,000,000
CR Cash ("B/S")	$37,200,000
CR Deferred Tax Credit ("B/S")	$2,800,000

Simple Example: Reporting Considerations - GAAP

FACTS:
Company purchases a credit of $40,000,000 for $37,200,000 in 2023. The Credit is used in full during 2023.

TO RECORD THE UTILIZATION	
(1) DR Taxes Payable ("B/S")	$40,000,000
CR Current Tax Benefit ("P/L")	$40,000,000
(2) DR Deferred Tax Expense ("P/L")	$40,000,000
CR Deferred Tax Asset ("B/S")	$40,000,000
(3) DR Deferred Tax Credit ("B/S")	$2,800,000
CR Deferred Tax Benefit ("P/L")	$2,800,000

Effective Tax Rate Example

FACTS:
Company purchases a credit of $40,000,000 for $37,200,000 in 2023. The Credit is used in full during 2023. The Company has a total federal tax liability of $100,000,000.

EFFECTIVE TAX RATE EXAMPLE	2023
Statutory Federal Income Tax Rate	21.00%
Transferable Federal Tax Credits [1]	(0.59%)
Effective Income Tax Rate	20.41%

[1] Pursuant to provisions under the Inflation Reduction Act, the Company purchased transferable federal tax credits during 2023 from a singular counterparty. Such federal tax credits were purchased at negotiated discounts, resulting in an income tax benefit recorded during the year utilized ended December 31, 2023.

Key Takeaways

1. **Know the rules**
2. **Understand your Company's risk tolerance**
3. **Socialization of benefits/risks**
4. **Modeling is key**
5. **Keep up to date**