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Carbon Capture Tax Credit Ruling Issued

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On July 1, 2021, the IRS issued Revenue Ruling 2021-13, allowing taxpayers that claim the carbon capture tax credit under Section 45Q to own part (but not all) of the carbon capture equipment. This important ruling clears the way for carbon sequestration projects to proceed by eliminating doubt about whether a taxpayer needs to own integral components of industrial facilities.

This client alert provides an overview of the carbon capture tax credit under Section 45Q and describes the new guidance.

General Requirements of the Credit

Section 45Q provides for a tax credit to the owner of carbon capture equipment that is originally placed in service at a qualified facility and used to capture qualified carbon oxide which is:

- disposed of in a secure geological storage;
- used as a tertiary injectant in a qualified enhanced oil or natural gas recovery (EOR) project and disposed of in a secure geological storage; or
- utilized in certain ways that result in emissions reductions as defined by federal requirements.

Carbon capture equipment includes property that is used to capture or process carbon oxide until it is transported for disposal or utilization. Such equipment generally includes components necessary to compress, treat, process, liquefy, pump or perform some other physical action to capture qualified carbon oxide, e.g., compressors, but generally does not include components of property used for transporting carbon oxide for disposal or utilization, e.g., pipelines.

A qualified facility is any industrial facility or direct air capture facility for which “construction begins” before January 1, 2026 (and for which the construction of carbon capture equipment also begins before that date or is part of the original design for the facility) and which captures during the year at least the following amounts of carbon oxide:

- 25,000 metric tons in the case of an industrial facility that emits no more than 500,000 metric tons of carbon oxide per year;
- 500,000 metric tons in the case of an electricity-generating facility; or
- 100,000 metric tons in the case of any other facility.

Unlike most other federal income tax credits, the taxpayer to whom a carbon capture tax credit is claimable can elect to transfer the credit to the person who disposes, uses or utilizes the carbon oxide in manner consistent with the requirements of Section 45Q.

Amount of the Credit

Although carbon capture tax credits have been available since 2008, amendments made to Section 45Q as part of the Bipartisan Budget Act of 2018 materially increased the amount and availability of the credit. For carbon captured using equipment originally placed in service at a qualified facility after February 9, 2018, taxpayers can receive a credit of up to:

- $50 (adjusted for inflation after 2026) per metric ton for carbon oxide that is captured and disposed of in secure storage; or
- $35 (adjusted for inflation after 2026) per metric ton of carbon oxide that is captured and either used by the taxpayer as a tertiary injectant in an EOR project or utilized.

Additionally, the credit for pre-February 9, 2018 facilities is subject to a national cap and scheduled to expire when 75 million metric tons of qualified carbon oxide have been taken into account under the rules. The credit for post-February 9, 2018 facilities is not subject to a national cap. Rather, it is available for the twelve-year period following the date that the carbon capture equipment is originally placed in service.

Revenue Ruling 2021-13

Revenue Ruling 2021-13 clarifies the following issues with respect to Section 45Q:

- That a single investor is not required to own every component of carbon capture equipment within a single process train in order to be eligible for Section 45Q tax credits;
- That the original placed-in-service date of a single process train of carbon capture equipment is the date that the single process train is placed in a state of readiness and available for purposes of generating Section 45Q tax credits; and
- That the placed-in-service date of a single process train does not affect the placed-in-service date of existing equipment for depreciation purposes.

The ruling considers an acid gas removal (AGR) unit installed at a methanol plant that was originally placed in service on January 1, 2017 for depreciation purposes. Since this date, the carbon oxide separated from the raw gas stream had been released into the atmosphere. In 2021, an investor purchases and installs new components of carbon capture equipment necessary to create a single process train capable of capturing the carbon oxide for transport. However, the investor does not acquire an interest in the AGR unit or the methanol plant.

The ruling concludes that, although the AGR unit's functions extend beyond the capture of carbon oxide (i.e., it is dual use property), it qualifies as carbon capture equipment for purposes of Section 45Q. However, the ruling also concludes that the investor is eligible for credits under Section

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45Q even though it does not own the AGR unit.

Although the AGR unit had been operational since 2017, it was not capable of capturing carbon oxide until the investor installed the new components in 2021 and, thus, was not placed in service for Section 45Q purposes until that time. However, despite this later placed-in-service date for Section 45Q purposes, the ruling concludes that the Section 45Q placed-in-service date has no effect on the placed-in-service date of each separate piece of equipment for depreciation purposes.
