IRA Tax Breaks May Reinforce Inequities, So We Need to Help

Four tax provisions could be used to include disadvantaged communities in the clean energy transition, but equity outcomes are unclear.

by Elizabeth Waters

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As our climate changes, it is becoming increasingly clear that our homes are more vulnerable to extreme weather than we thought. Flooding, wildfire, heat, and rising energy costs make the stability of our homes and communities feel tenuous. These effects are most acute and immediate for people living in low-income communities and communities of color, who—because of a complex suite of factors, including where they live, the quality of their homes, and the high cost of utilities—are less able to prepare for and recover from extreme weather events and rising temperatures.

Approximately 16% of the investments in the Inflation Reduction Act (IRA) go toward environmental justice initiatives. Within that, four tax provisions could be leveraged to provide the affordable housing sector with access to clean energy and home efficiency improvements:

- The Low-Income Communities Bonus Credit Program (48e), for which the U.S. Department of the Treasury released new guidance in February 2023
- The New Energy-Efficient Homes Tax Credit (45L)
- The Energy-Efficiency Home Improvement Credit (25C)
- The Residential Clean Energy Credit (25D)

Low-Income Communities Bonus Credit Program: 2023 Allocations

	Category	Bonus Credit	2023 Allocation
1	Facility is located in a low-income community	10%	700 megawatts
2	Facility is located on Tribal land	10%	200 megawatts
3	Facility is part of a federally subsidized, low-income residential building project, including housing supported by LIHTC and Section 8 of the Housing Act	20%	200 megawatts
4	Facility is part of a qualified low-income economic benefit project	20%	700 megawatts

Source: U.S. Department of the Treasury

Together, the provisions could help reduce energy burdens and increase the resilience of low-income communities. However, the extent to which they will achieve this depends on whether further guidance prioritizes the equitable allocation of benefits. It is imperative that affordable housing stakeholders, including building industry professionals, are aware of, advocate for, and prepare for equitable outcomes.

"Climate issues are social justice issues"

The affordable housing sector impacts and is impacted by climate change. According to an IRA policy brief by the National Housing Trust, annual onsite energy usage across the portfolio of the U.S. Department of Housing and Urban Development (HUD) generates approximately 13.6 million metric tons of greenhouse gas emissions. Furthermore, a 2021 study from the U.S. Environmental Protection Agency (EPA) shows that socially vulnerable groups—particularly low-income communities of color—are the most heavily impacted by the effects of climate change, reporting a higher-than-average incidence of childhood asthma due to low air quality, deaths and loss of work hours from extreme heat, and property damage from flooding.

Low-income communities are more likely to be located in the most vulnerable areas, a fact linked to discriminatory policies, such as redlining, explained Ayate Temsamani, a senior policy analyst at Enterprise Community Partners, a national affordable housing nonprofit. “The residents in these communities, because of their financial limitations, also tend to live in low-quality homes that are less stable,” she continued. Because of this, they “face higher energy burdens, which is being exacerbated as temperatures rise and utility expenses increase.”

A study by Eric Scheier and Noah Kittner published in *Nature Communications* in 2022, found that 16% of U.S. households experienced energy impoverishment, paying more than 6% of their income toward energy, with Black, Hispanic, and Native American communities—and renters—disproportionately affected. The National Housing Trust notes that energy, as one of affordable housing’s highest controllable operating costs, can affect a building owner’s ability to invest in building-wide improvements and provide affordable rents.

As Temsamani states, “I can’t stress this enough: climate issues are social justice issues.”

Tax provisions in the IRA related to affordable housing

Achieving sustainability and resilience in low-income communities will require expanding their access to clean, affordable energy and well-built, efficient infrastructure. But this is costly. Dirk Wallace, a certified public accountant and partner at Novogradac, a public accounting firm, explains that securing financing for a property can be a challenge, and “plenty of times, there is a financing gap.” He says that although many states are requiring efficiency, developers are often unable to secure the financing they need to defray the associated upfront costs. The four tax provisions discussed in this article aim to address this.

The Low-Income Communities Bonus Credit Program (48e)

The Low-Income Communities Bonus Credit Program is a new tax provision that adds a bonus credit to the Investment Tax Credit (ITC), which the IRA extends until 2025 (when the Clean Electricity Investment Tax Credit will replace it.) The ITC provides a base credit of 6% for qualified projects and up to 30% for those that meet prevailing wage and registered apprenticeship requirements or are under one megawatt. It offers two additional, stackable 10% bonus credits for projects that meet domestic content requirements for steel, iron, and other manufactured materials or for those located in an “energy community.”

The Low-Income Communities Bonus Credit offers a further credit (stackable with the others in the ITC) for small-scale solar and wind facilities located in low-income communities and those with environmental justice concerns. The intention of the credit is to drive social and economic benefits to these communities through adoption of and access to renewable energy. Eligible facilities must produce under five megawatts of energy and fall within one of four categories. Recent guidance from Treasury announced 2023 capacity allocations, which total 1.8 gigawatts (see table).

Wallace is optimistic that this bonus

structure will work as intended: "Since that bonus is something an investor (most likely a developer that is going to monetize and build renewable energy) is going to purchase, using adders to make sure projects are done in low-income communities [will mean] the ultimate recipients of the energy are going to be low-income individuals," he told BuildingGreen. "The general consensus is that [renewable electricity] would be cheaper on average across the country."

Still, Wallace notes, outcomes will depend upon the nature of the forthcoming guidance. Treasury should be releasing further funding criteria by the third quarter of 2023, when it says it will begin accepting applications for categories 3 and 4.

The New Energy-Efficient Homes Tax Credit (45L)

The New Energy Efficient Homes Tax Credit is an existing provision that the IRA expanded and extended until 2032. It offers homebuilders a credit range of $500 to $5,000 per unit for homes that meet current Energy Star or Zero-Energy-Ready Home energy performance standards and prevailing wage requirements. Wallace believes that "we are going to see [45L] on most affordable housing projects now. I think everyone understands the standards a lot better, and most states are requiring [them]. I've never heard as much talk as I have now on the solar credit."

Additionally, for properties that receive the Low-Income Housing Tax Credit (LIHTC), receipt of funding through either provision 48e or 45L will not reduce the value of capital investment eligible for LIHTC credit.

Energy-Efficiency Home Improvement Credit (25C) and Residential Clean Energy Credit (25D)

Sections 25C and 25D are extensions and expansions of existing provisions. Under section 25C, homeowners, and sometimes renters, are eligible for a 30% tax credit for various efficiency improvements. 25D offers homeowners and renters credit to install residential clean energy equipment: 30% through 2032, 26% in 2033, and 22% in 2034, expiring at the end of that year.

Improving the efficiency of residential buildings and providing them with on-site clean energy is necessary to reduce energy impoverishment and increase climate resilience. Unfortunately, these two credits do not have "direct pay" options, which, argues Lew Daly at the Roosevelt Institute, a progressive think tank, "means that approximately 40% of households with little or no federal income tax liability—disproportionately people of color—will continue to be largely excluded from installing rooftop solar, heat pumps, and other clean energy resources."

Tax credits tend to exacerbate inequality

Daly writes, "Tax credits tend to reproduce, not reduce, existing economic inequities, especially by race, and the IRA does not do enough to address this problem."

In an issue brief published by the Roosevelt Institute, Daly and Sylvia Chi of the Just Solutions Collective, assert that tax credits, often used in the pursuit of social goals in the U.S., have historically benefited white, affluent people. They argue that the uneven distribution of benefits, coupled with the fact that tax credits replace collective decision-making with private choice, undermine public power and make it hard to correct inequalities.

Though the IRA does not fix these issues, it takes steps in certain provisions, including 48e and 45L, to build social justice outcomes into tax credits. As Todd Tucker and Sunny Malhotra discuss in another piece published by the

Roosevelt Institute, these provisions "attach many of the types of conditions that have historically only been linked to direct government procurement and grants for goods and services." Adding social justice conditions to tax credits allows the federal government to steer private-sector investment and could make the federal government's role more visible to the general public.

But the guidance for tax incentives needs to be further honed to ensure benefits reach low-income communities and households. In comments submitted to Treasury about implementation of the tax incentives in the IRA, 50 equity and environmental justice groups, community-based organizations, and coalitions outlined the steps the agency should take to ensure the most disadvantaged communities benefit from the provisions and are not left behind. Among many other requests, the letter asks Treasury to address the equity gap that's exacerbated by inaccessible tax breaks and to include clean energy tax incentives under the Justice40 Initiative, an executive order that pledges 40% of the benefits of certain climate-related federal investments will go to disadvantaged communities. Regarding 48e, it requests that the agency prioritize projects that center community partnership and engagement during development and that drive the largest benefits to low-income people. The comments also request a clear definition of "financial benefits," a term used in the initial guidance for 48e. They ask Treasury to outline exactly what the financial benefits to residents will be, and how they will be measured.

The building industry can prepare and advocate for equity

Wallace advises professionals in the building industry to get familiar with new energy performance standards and to make sure their properties meet the energy requirements laid out in the IRA. He asks them to consider, "What can you do now to save you money in the future when we finally get guidance?"

Temsamani explained that Enterprise "really encourages our partners or any stakeholders to continue to weigh in with recommendations that dollars flow effectively and efficiently through their subject-matter lens." She added, "We strongly recommend that those in the housing sector work to establish a relationship with state energy offices."

As agencies continue to develop guidance for these (and many other) provisions, building professionals can let them know that equity and access for historically marginalized communities are priorities.

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