

Direct Pay: Supporting Decarbonization of State and Municipal Governments

Through the Inflation Reduction Act of 2022, clean energy tax credits for technologies such as solar, geothermal and EV charging are now accessible to state and local governments and other tax-exempt entities.* This is possible through what is known as direct pay, where state and local governments and other tax-exempt entities can get reimbursed up to 50 percent for the cost of clean energy projects once projects are completed.

What Is Direct Pay?

In simple terms, direct pay (also known as elective pay) is a mechanism that lets tax-exempt entities, including state and local governments, to recoup a significant portion of the cost of a clean energy project as a reimbursement from the IRS. Historically, it wasn't possible for state and local governments and other tax-exempt entities to take advantage of clean energy tax credits. Now, thanks to the Inflation Reduction Act and the novel inclusion of direct pay, state and local governments can receive the full value of a clean energy tax credit as cash payment once a project is placed in service.

What Qualifies for Direct Pay?

There are a total of 12 clean energy tax credits where direct pay is applicable. However, the clean energy tax credit most relevant to decarbonizing municipal buildings is the Clean Electricity Investment Tax Credit (48E/48), while 30C for EV charging stations and 45W for EV buses or fleets are also relevant for state and local governments.

- Solar panels (48E)
- Battery storage (48E)
- Thermal energy storage (48E)
- Geothermal heat pumps (48)
- EV charging stations (30C)
- EV school buses (45W)

HVAC sidenote: Geothermal heat pump systems (also referred to as ground source heat pumps) can serve as replacements for traditional HVAC systems and can cut energy bills by up to 65 percent.ⁱ In addition, heat pumps can provide improved indoor air quality and provide better temperature control.

The Payoffs

- Direct pay reimbursements can be reinvested back into the budget to help cover expenses such as operational, maintenance, capital and staffing costs.
- Additional money comes from annual energy savings from installing clean energy technologies.

*Under the final regulations, any organization described in sections 501 through 530 of the Code that meets the requirements to be recognized as exempt from tax under those sections is an applicable entity eligible to make an elective payment election. <https://public-inspection.federalregister.gov/2024-04604.pdf>

- HVAC upgrades and EV buses lead to improvements to indoor and outdoor air quality, supporting the health of your staff and the broader community.
- Municipal buildings powered by renewable energy and battery storage can create climate resilient hubs during power outages.
- Upgrading municipal buildings will create good jobs and job training opportunities in the local community.
- Upgrading municipal buildings will contribute to emissions reductions goals at the local and state levels.

Recommended Next Steps

1. Build your support network: Coordinate with your state energy office, state education agency, state department of commerce, local sustainability office and/or local utility to learn about additional available funds, see local examples and get technical assistance.
2. Identify upfront financing: This may include municipal bonds, state grant programs, utility rebates, state green banks, credit unions, community development finance institutions and energy service companies.

Additional Resources

- BlueGreen Alliance: [Making Clean Energy Tax Credits Deliver for the Public](#)
- Lawyers for Good Government: [Clean Energy Tax Navigator](#)
- Local Infrastructure Hub: [Direct Pay Full Report](#)
- S2 Strategies: [State Support Center](#)

Additional Considerations

With the shifting priorities of a new administration, the clean energy tax credits may become a target. Here's what we know: Because these clean energy tax credits are the law of the land, any attempt to challenge these credits must be done by passing a new law through Congress and not through executive orders. To stay up to date on the continued availability of direct pay, go [here](#).

For questions or to learn more about direct pay, contact:

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Case study

The city of Madison, Wis., expects over \$13 million in direct pay reimbursements to help finance sustainability improvements to municipal and community facilities. This includes solar installations at the Community Development Authority's Truax Campus and geothermal systems at multiple facilities, including a men's homeless shelter, the Imagination Center at Reindahl Park, the Far West Streets Facility, and the Police Property and Evidence Facility and South District Station.ⁱⁱ

ⁱ www.energy.gov/eere/articles/5-things-you-should-know-about-geothermal-heat-pumps

ⁱⁱ www.cityofmadison.com/finance/documents/budget/2024/capital/executive/ExecutiveSummaryFinal.pdf