Coupling Inflation Reduction and Energy Transformation

by: Kenneth J. Warren / *The Legal Intelligencer*

On June 30, the U.S. Supreme Court limited the authority of the U.S. Environmental Protection Agency (EPA) to utilize the Clean Air Act to shift electric power production to sources with lower greenhouse gas emissions. Relying on the "major questions doctrine," the court in *West Virginia v. EPA* held that in the absence of clear Congressional authorization, the EPA could not lawfully promulgate regulations that would transform a sector of the economy by requiring coal-fired power plants to reduce their production or to subsidize natural gas, wind or solar sources. The Supreme Court thus returned the climate debate to a reluctant Congress.

Meanwhile, the economy was suffering from levels of inflation unseen in many decades. The public consternation over inflation created political jeopardy for the president and Democrats in Congress whom the public blamed for higher prices of food, gasoline and other items. Inflation reinforced the objections of Sen. Joe Manchin of West Virginia to the Democrats' Build Back Better plan that carried estimates in excess of $2 trillion to fund its climate change and other programs.

Build Back Better was the vehicle the Democrats chose to advance their climate agenda over Republican objections. By using the Congressional budget reconciliation process, a majority vote in the Senate could avoid a filibuster. But the absence of unity in the Democratic senatorial caucus or the support of any Republican senator slammed the door on Build Back Better. This appeared to strike a fatal blow to climate legislation in this session of Congress.

Enter the Inflation Reduction Act of 2022 (IRA). In a stunning agreement negotiated between Manchin and Senate Majority Leader Charles Schumer, the Democrats propose to adopt tax, health care and energy legislation that will reduce the deficit and seek to lower prices throughout the economy. Employing Congressional tax and spend authority to address climate far more comprehensively than did the Clean Power Plan at issue in the *West Virginia* decision, the proposed legislation offers incentives to transform and decarbonize energy production throughout the economy.

Whether the corporate minimum tax, Medicare, energy, or other provisions of the IRA will materially reduce inflation is contested. The fact that the IRA's investment of $369 billion in energy security and climate change mitigation and adaptation would have a material, lasting effect on energy production and use is apparent. According to Schumer, the clean energy provisions of the IRA will reduce domestic greenhouse gas emissions by approximately 40% by 2030.

For climate advocates with different preferences on how to decarbonize the economy and reduce greenhouse gas emissions, the IRA has something for everyone. It extends existing tax credits and creates new tax credits and grants. Although a full summary of the 725-page IRA is beyond the scope of this article, a focus on some of the climate highlights illustrates the breadth of the bill and its potential transformative effect on our economy.

The IRA seeks to modernize transportation, the sector of our economy producing the greatest amount of greenhouse gases. The now-familiar tax credits for consumers to purchase electric vehicles are extended; $4,000 for used electric vehicles (EVs) and $7,500 for new EVs will be available to consumers whose income fall below thresholds ($300,000 of modified gross income on joint returns for purchasers of new EVs). Certain made or assembled in America requirements apply to vehicle battery components and other limitations apply to the origin of critical materials. Significant funds or tax credits are also available for installing emissions equipment at airports and ports, and for constructing electric and other alternative fuel charging stations. Funds are provided for postal service clean fleets, and incentives are offered for production of clean transportation fuels, including hydrogen produced by sources with zero or low emissions.

The IRA also encourages individuals to make clean energy and efficiency improvements to their homes. Consumers who purchase energy efficient appliances, windows, doors and heat pumps or perform home energy audits are entitled to specific tax credits or rebates. Similarly, building owners are rewarded for investing in efficiency and electrification. And local governments are provided funds to develop zero building energy codes.

The IRA also offers tax incentives for production of or investment in clean energy. A manufacturing production tax credit is available for wind energy components, solar cells, battery storage and inverters. Energy storage systems, grid modernization equipment, energy conservation projects, carbon capture projects and other advanced energy initiatives are also eligible for tax credits. Credits or grants are available for building or retooling clean technology or automobile manufacturing facilities. Electric generators who produce no greenhouse gases because they utilize solar, wind, nuclear, or carbon recapture technologies are likewise entitled to tax benefits. The inclusion of nuclear power constitutes an affirmation of its importance when transitioning to zero-emission electric generation.

The IRA also invests in agriculture and forestry. Conservation investments are available to improve soil carbon, to capture and sequester greenhouse gases and reduce nitrogen loss, and to mitigate climate change. Incentives are granted for biofuel production and infrastructure. In addition, grants are offered for climate mitigation, carbon sequestration, resilience and fuel reduction in forests. Renewable energy loans are available for rural developments.

As a compromise to secure the vote of Manchin, the IRA does not penalize fossil fuels. It does, however, provide incentives and charges to reduce methane emissions from oil and gas systems. Although investments in all fuel types, including fossil fuels, renewable, hydrogen, geothermal, nuclear and energy storage, are contemplated, the IRA adjusts incentives over time to allow the market to determine which fuel types become prevalent. And recognizing the potential confusion engendered by corporate claims of sustainable operations, the IRA provides funds to the EPA to standardize corporate climate action commitments.

The energy and environmental provisions of the IRA reflect the Biden administration's pursuit of environmental justice. The IRA provides grants for financial and technical assistance to low-income and disadvantaged communities through the Greenhouse Gas Reduction Fund and environmental and climate justice block grants. It appropriates funds to promote energy efficiency and resilience in affordable housing, and provides enhanced energy credits for solar and wind facilities placed in service in low-income communities. It offers energy efficiency rebates to low and moderate-income households. It includes drought response and preparedness funds for disadvantaged communities and provides funds for the Council of Environmental Quality to collect data on the disproportionate effects of climate impacts. It is questionable whether the IRA contains sufficient incentives to construct the additional transmission lines needed to accommodate new renewable energy sources and increased demand for electricity resulting from converting vehicles, homes and buildings to electric power. Although the IRA provides some incentives to improve the electric grid, facilitate transmission line siting and increase equipment efficiency, greater attention to matching transmission line availability with electric generation capacity may be needed.

The details of commitments made to Manchin for future actions to streamline permitting, including for new oil and gas pipelines, may raise further concern. Speeding reviews under the National Environmental Policy Act (NEPA) required for major federal actions affecting the environment may clear roadblocks for both oil and gas projects and renewable energy projects. The environmental community may bristle at NEPA changes that facilitate projects they dislike, even though the changes may also speed approval of projects they favor. The Biden administration may be willing to pay this price to advance its climate goals.

Passage of the IRA is not assured, and its provisions will be reviewed by the Senate Parliamentarian to determine whether they meet the tax and spend criteria for a budget reconciliation bill. Nevertheless, the climate provisions appear to have been carefully crafted as tax incentives and appropriations to survive the reconciliation process. Passage of the IRA may be our nation's best hope for prompt action to mitigate the effects of climate change.

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