STATE INNOVATION EXCHANGE

CONGRESSIONAL PROGRESSIVE CAUCUS CENTER

A STATE LEGISLATOR'S GUIDE TO DIRECT PAY:

BUILDING JOBS & SUSTAINABLE PUBLIC ENERGY

Contents

Executive Summary

The Inflation Reduction Act (IRA) includes Direct Pay tax credits that have the potential to bring nearly unlimited funding for clean energy projects into the communities that need them most. Direct Pay tax credits will **radically expand publicly owned energy, support communities transitioning away from polluting energy sources, generate affordable—and potentially free—electricity, and create good jobs for local communities.**

This guide is designed to help state lawmakers seize this historic opportunity for their communities through:

1. **Community education and outreach:** State legislators are trusted messengers who can **spread the word** about this opportunity to local governments, community organizations, and other eligible entities within their state.

2. **Implementation:** State legislators can ensure that the state government enthusiastically **implements the IRA** and secures Direct Pay funding for their state by implementing eligible projects across all levels of state government.

3. **Funding and policy making:** State legislators can **help other eligible entities like local governments and nonprofits implement Direct Pay** projects by providing matching funds, creating revolving funds or low/no-interest loans, creating technical assistance programs, and building in policy incentives to increase equity and protect workers within Direct Pay programs in the state.

Direct Pay tax credits are available to tax-exempt entities like state governments, local governments, schools, hospitals, public utilities, houses of worship, and nonprofit organizations for the first time ever. Direct Pay tax credits can fund a wide range of renewable energy projects like solar arrays, wind turbines, electric vehicle (EV) charging infrastructure, and storage resources like batteries. Every project that meets the Direct Pay requirements will receive the tax credit, so communities can implement project after project without competing for limited and dwindling funds. However, it will take robust leadership from state-level elected champions to fully realize this opportunity.

State governments can receive Direct Pay tax credits, which can provide significant funding for state-owned green energy projects and can be used on an uncapped number of qualifying projects. In addition, state governments have a critical role to play in ensuring that state residents understand this opportunity and have the knowledge, financing, and technical support needed to seize this opportunity through policies like grants, revolving funds, and technical assistance. This guide is intended for state governments to use and to better understand how to use Direct Pay to help expand resilient, sustainable energy, lower energy costs, take action on the climate crisis, and create good-paying local jobs.

SECTION 1:
ABOUT DIRECT PAY

For the first time ever, thanks to the IRA, the federal government will give **tax-free direct cash funding** to tax-exempt entities like state governments, local governments, schools, hospitals, public utilities, houses of worship, and nonprofit organizations to build renewable energy projects like solar arrays, wind turbines, EV charging infrastructure, and storage resources like batteries. This provision—called Direct Pay, or sometimes Elective Pay—gives tax-free cash payments from the IRS. These Direct Pay tax credits create an opportunity to **radically expand publicly owned energy, support communities transitioning away from polluting energy sources, generate affordable—and potentially free—electricity, and create good jobs for local communities.**

UNDERSTANDING THE FUNDING AVAILABLE THROUGH DIRECT PAY

The funding available through Direct Pay can be unlimited! Direct Pay funds come in the form of refundable tax credits. Since eligible entities like state governments are tax-exempt, the tax credits are cash payments from the federal government and are paid directly to the eligible entity once the project begins generating energy. The credits last until 2032, and once the IRS determines that the project qualifies, the eligible entity will receive **direct tax-free funds covering 30% to 70% of the project costs or an amount for each kilowatt generated**. Every project that completes a pre-filing process and meets the IRS' requirements will get Direct Pay funds. Projects that meet worker protection standards, buy American-made materials, and support communities with the greatest need will also qualify for more funding.

The state governments, cities, counties, nonprofit organizations, and other eligible entities can all access this funding simultaneously and do not need to compete with each other for it. Eligible entities are not limited in the number of eligible projects they can undertake. For example, state governments could put solar panels on state-owned buildings, invest in EV charging infrastructure for state fleets, and create a program to build state-owned solar panels and wind turbines in communities across the state. Each of these projects would be eligible for Direct Pay funding once completed, and there is no limit to the number of eligible projects that the state could complete.

EXPANDING RACIAL AND ECONOMIC JUSTICE THROUGH DIRECT PAY

Creating Good Green Jobs

Eligible entities can maximize economic justice for working people by meeting the IRA's requirements to pay workers a prevailing wage and use registered apprentices on projects so workers get the training they need to build careers. State and local governments can also ensure their projects create safe, high-quality jobs and that projects stay on time and budget by using union labor. State governments can also maximize their impact on economic justice by attaching additional worker protection requirements for Direct Pay-eligible projects that receive state grants or state technical assistance. See the Congressional Progressive Caucus Center's (CPCC) **FAQs on How to Protect Direct Pay Project Workers** and **Guide to IRA Worker Protection Requirements** for more information.

Lowering Energy Burdens

In addition to creating good green jobs, states can use Direct Pay to increase economic and racial justice by lowering the burden of high energy costs on low-income households. Twenty-five percent of all U.S. households struggle with a high energy burden (i.e., spend more than 6% of their income on energy bills), and 67% of low-income households face a high energy burden. Black households have a 43% higher rate of energy burden compared to non-Hispanic white households. Native American households face a 45% higher burden, and Hispanic households face a 20% higher burden than non-Hispanic white households. Renters and older people also face disproportionate burdens. Publicly owned clean energy infrastructure can play a critical role in lowering energy costs for households struggling to afford to heat and cool their homes because publicly owned energy can serve the public interest rather than shareholder profits, keeping costs down.

Addressing Environmental Racism

Governments can maximize racial justice by taking on projects that serve the communities that have been hardest hit by racist policies, fossil fuel extraction, and pollution. Black, Indigenous, and other people of color are more likely to live in communities with high pollution burden, that are near dirty power plants, or that are facing catastrophic harm in the climate crisis. For example, the American Lung Association found that people of color are 3.7 times more likely than white people to live in a county with high levels of air pollution. People of color are also disproportionately likely to live in areas affected by heat or flooding and work in occupations where they are exposed to toxic conditions. A rapid and just green energy transition is critical to achieving racial justice.

The unprecedented funding offered by Direct Pay is a critical opportunity to begin investing in the communities that have borne the greatest burden under the current extractive energy economy. For example, a state government might build publicly owned resilient power in communities prone to blackouts and outages. Similarly, a state government could build publicly owned utility-scale renewable energy projects to transition away from coal-fired power plants, install community solar for public housing units, or install public EV charging stations in frontline communities.

Redressing Redlining and Bluelining

Environmental racism subjects communities of color to higher rates of toxic exposure and climate risk. Decades of disinvestment and racist policies like redlining also mean that these same communities are more likely to need help securing the up-front funding to pay for green energy projects. The impact of disinvestment and redlining is magnified in many communities by bluelining and systematic financial discrimination against communities because of perceived environmental risk. This financial discrimination could prevent communities of color and low-income communities from securing the financial resources to build clean energy infrastructure and benefit from the green energy economy. State governments can play an important role in ensuring an equitable implementation of Direct Pay by creating grant programs or revolving funds that provide no-cost or low-cost funding for green energy projects, especially by reserving funding for projects serving communities of color and other environmental justice communities.

Centering Community Voices

Direct Pay is a perfect opportunity to engage directly with frontline communities so that state-run and state-funded projects reflect the needs and demands of communities themselves. Governments can also prioritize workers of color when hiring for Direct Pay project jobs. Tools like pre-hire collective bargaining agreements can include hiring targets for workers of color, women, workers with disabilities, or veterans. These agreements bring jobs to target communities and shrink racial and gender pay disparities.

THE ROLE FOR STATE ELECTED CHAMPIONS

State-level elected champions can help their communities seize this historic opportunity in **three key ways**:

1. **Community education and outreach:** State legislators are important and trusted messengers **who can spread the word** about this opportunity to local governments, community organizations, and other eligible entities within their state.
2. **Implementation:** State legislators can ensure that the state government enthusiastically **implements the IRA** and pursues Direct Pay projects across the state government and state agencies.
3. **Funding and policy making:** State legislators can use their **policy-making function to help other eligible entities implement Direct Pay** projects by providing matching funds, creating revolving funds or low/no-interest loans, creating technical assistance programs, and building in incentives to increase equity and protect workers within Direct Pay programs in the state.

SECTION 2:
COMMUNITY EDUCATION AND OUTREACH

Many eligible entities are unaware of the Direct Pay provision in the IRA and its potential to create good green union jobs, lower energy costs, clean up our air and water, and more. State legislators are trusted messengers who can help spread the word about this opportunity to city and county governments and other eligible entities among their constituencies, including school districts, public universities, nonprofit hospitals, houses of worship, and nonprofit community organizations.

Opportunities to spread the word about Direct Pay include:

- Host a town hall or public meeting on Direct Pay opportunities in your community.
- Host a meeting with city and county officials, school board members, key community groups, and leaders of key anchor institutions in your district, such as large public universities, nonprofit hospitals, and school districts, to encourage them to take action with Direct Pay.
- Host a meeting with utilities serving your district to encourage them to actively support Direct Pay projects by making interconnection agreements simple and equitable.
- Host a meeting with local community foundations and other local philanthropists to encourage them to offer grants and funding to support the construction of Direct Pay projects by small eligible entities.
- Share information about Direct Pay on social media.

SAMPLE DIRECT PAY COMMUNICATIONS MATERIALS

- The CPCC has created a partner toolkit on Direct Pay that includes sample messaging, sample social media posts, shareable graphics, and a shareable video explaining Direct Pay.
- CPCC has created a sample presentation on Direct Pay that you are free to use without attribution or adapt for your purposes however you see fit.

SECTION 3:
STATE IMPLEMENTATION

State governments and state agencies are eligible entities under the Direct Pay provisions. The scale of projects possible at the state level helps ensure that the promise of the IRA is made real.

Example state-level sustainable Direct Pay projects:

- A state implements a 100% clean energy plan or other climate action plan and uses Direct Pay to supplement the cost of implementing widespread clean energy projects across the state. According to the Initiative for Energy Justice's Environmental Justice Scorecard, New York's Climate Leadership and Community Protection Act (SB 6599) and Washington's Clean Energy Transformation Act (SB 5116) reflected more environmental justice principles in the creation, implementation, and design of their programs than most existing state 100% clean energy plans. Many of the plans envisioned in these laws would now qualify (at least in part) for Direct Pay tax credits.

- A state uses Direct Pay to supplement the cost of electrifying the state fleet through building out solar-powered EV charging infrastructure for state-owned and -operated vehicles. Oregon, Hawaii, Minnesota, and Washington have announced plans to electrify state fleets. Today, building EV charging infrastructure as part of those plans would be eligible for Direct Pay tax credits, and many other parts of the IRA include funding for clean vehicles that could further supplement these plans.

- A school district in Batesville, Arkansas, installed solar panels and made its buildings more energy efficient, saving nearly $300,000 per year. The district then used the money saved to raise teacher pay. Today, adding solar panels to school buildings or other state-, city-, or county-owned buildings would also qualify for a Direct Pay tax credit, reducing the cost of the initial investment and creating even more savings that can be applied to teacher pay or other critical community priorities.

- A state puts solar panels on state-owned buildings from the state house to state agencies, creating good green jobs and lowering energy costs for the state. States can add solar, wind, or other clean energy infrastructure to state-owned buildings directly and claim Direct Pay tax credits or create grant programs to add clean energy infrastructure to other publicly owned buildings.

- A state housing agency updates public housing and affordable housing units, including adding rooftop solar to lower energy costs. For example, investments in public housing such as the Massachusetts' Affordable Homes Act could be expanded using Direct Pay.

- A state supports state-funded schools to transition to electric buses by matching federal funds to transition local bus fleets and building solar-powered charging stations on school property. For example, Delaware and Maryland are among the states that are moving toward school bus electrification. The school system saves money and reduces dangerous diesel emissions that put our kids at risk. The school system would be able to claim a reimbursement for up to 70% of total project costs with Direct Pay credits for building EV charging stations and solar panels to help offset the costs of transitioning the school bus fleet and could match that with other federal funding for the purchase of electric vehicles.
- A state builds publicly owned utility-scale renewable energy projects on state-owned land, including Brownfield land or equity-focused community solar projects, and uses that clean energy to transition away from coal- and natural gas-fired power plants.

SECTION 4: **STATE POLICY, FUNDING, AND INCENTIVES**

Eligible entities will face a number of challenges in seizing the Direct Pay opportunity, including navigating an unfamiliar process with the IRS, planning and implementing sometimes complex energy projects, and finding the up-front capital to cover the cost of construction and bridge the difference between project costs and the portion eligible for Direct Pay funds. State legislators have a central role in ensuring that their communities can fully embrace this opportunity to take urgent action on the climate crisis, lower energy costs, clean up our air and water, and create good-paying green jobs.

Beyond ensuring that state governments implement Direct Pay-eligible programs, state legislators have the opportunity to help other eligible entities make the benefits of the IRA real in their communities by using state funding and state policymaking tools to help other entities access Direct Pay tax credits. Policies like those that call for 100% sustainable energy by 2030 create the demand and market assurance necessary to fully maximize the benefits of the IRA, but only if they are created and implemented with a central focus on improving life for communities on the frontlines of the extractive energy economy and the climate crisis. This must include community participation in the lawmaking and implementation process and significant, measurable, and enforceable programs designed to restore the communities that have been most harmed.

Providing matching funding will be especially critical for communities with the least access to resources, including frontline and fenceline communities, communities of color, communities transitioning away from extractive economies, rural communities, and low-income communities. Below, we outline some possible examples of Direct Pay financing. We plan to update this when we have more information from the federal government.

FUNDING FOR DIRECT PAY PROJECTS

While Direct Pay tax credits can provide substantial funding for renewable energy projects, these projects will need additional funds to cover the full project completion costs. Eligible entities will have to cover the cost of project construction before they receive the tax credit. Depending on the exact Direct Pay tax credit, the payment will either be disbursed as a one-time credit covering between 6% and 70% of total project costs when the project is completed or as a payment based on electricity production over ten years. To learn more about the structure of the specific tax credits, see the CPCC's in-depth explanation of how the investment tax credit (ITC), the production tax credit (PTC), and other bonus credits work here. The Center for Public Enterprise has produced a financial model that makes it possible to compare the ITC and the PTC for a planned project.

Many under-resourced communities must raise funds to complete a project before Direct Pay funding is available, which poses a significant obstacle. Access to reliable public funding to match federal funds is necessary for many communities to access the benefits of Direct Pay, or they may be vulnerable to predatory lending. State governments can dramatically increase the reach of the Direct Pay tax credits by providing direct funding through grants and by helping local governments and other eligible entities find safe, reliable, and low-cost financing options that do not undermine the public nature of the ownership of these new sustainable energy generation assets.

State funding for Direct Pay-eligible projects increases equity and justice in implementation by adding additional incentives or requirements to target funds toward projects that create good local union jobs and projects that serve frontline communities. The federal government set the floor with the IRA. Now, state legislators can break through the ceiling in achieving maximized benefits for vulnerable communities, the environment, and workers. For example, it is critical to prioritize projects that include community input and reflect community demands rather than simply defining projects by geography, which may unintentionally result in funding projects that disempower or further harm frontline communities. For more information on how to define environmental justice communities in order to prioritize funding for the communities that have been harmed the most, see the Climate and Clean Energy Equity Fund's report on defining environmental justice communities in policy.

Truly just and equitable implementation of Direct Pay will only be possible if policymakers ensure that frontline communities have access to nonpredatory funding. State policymakers can play a critical role in expanding access to Direct Pay in a number of ways, including:

Direct State Funding

States can appropriate funding for grants to local governments or other eligible entities to cover the up-front costs of projects. States can maximize equity and justice in implementation by requiring projects that receive state funds to meet higher labor and community benefit standards. Additionally, they can prioritize grants for the communities that need them most, such as frontline communities and communities of color.

For example, several states have implemented grant programs to fund clean energy projects. Washington State's Department of Commerce provides grants for school sustainability, and Minnesota has proposed a grant program to support the installation of solar panels on public buildings. Minnesota also established a state competitiveness grant fund to award grants to local and tribal governments, utilities, nonprofits, and other eligible entities when they required matching funds to access IRA funds. This type of state grant program is critical because it allows local governments or community nonprofits to finance their projects, and Direct Pay ensures that state funds go further.

State Revolving Funds

To maximize state funds, states could provide funding in the form of a no- or low-cost loan from a revolving fund. While there is not a federally created revolving fund for clean energy, states can establish their own revolving funds to finance clean energy projects. Direct Pay makes those revolving funds considerably less risky, as eligible entities will have a head start on repayment with their Direct Pay reimbursement funds. A no- or low-cost revolving loan fund could work as follows:

1. A state establishes a no- or low-cost revolving loan fund for local governments, tribal governments, and nonprofit entities within the state. States can add additional worker protections, community participation, and targeting for projects serving the hardest hit communities to the loan fund.
2. Eligible entities apply to the state for a loan and use the loan funds to complete their project.
3. The eligible entity pre-files with the IRS once their project is near completion and then applies for Direct Pay tax credits once their project is completed.
4. The eligible entity receives their Direct Pay funds from the IRS and can apply that toward repaying their loan to the state.
5. The state reinvests in the next eligible project.

Many states already have an energy loan fund that supports the generation of clean energy projects or energy retrofits within the state. These loan funds could be expanded or modified to create more opportunities to fund Direct Pay-eligible projects and accelerate the clean energy economy. For example, Texas' LoanSTAR Revolving Loan Fund currently supports energy efficiency retrofits but could be easily expanded to include Direct Pay-eligible EV charging stations and energy generation projects like rooftop solar or wind turbines.

State and Municipal Bonds for Matching Funds

States, cities, and other government entities can authorize the use of bonds to cover the costs of Direct Pay-eligible projects. States can use bonds to fund state-owned Direct Pay projects or authorize bonds to collectively fund smaller projects at the local level. More information on using bonds for renewable energy is available in the Department of Energy bond resource guide for state and local officials.

In 2024, California voters will vote on a ballot measure to authorize $15.5 billion in bonds to finance projects for climate resilience, extreme heat mitigation, and clean energy programs, including a $500 million appropriation to the State Energy Resources Conservation and Development Commission for grants to assist in obtaining or receiving a state match to regional hubs for IRA funds. In addition to securing federal grant funds, many of the projects financed by this bond, if it passes, may be eligible for Direct Pay.

State Green Banks

Some states have Green Banks, which are financial institutions designed to lower energy costs and encourage the construction of sustainable energy infrastructure by blending public and private capital and financing a broad range of sustainable energy projects. While "Green Bank" is often used as an umbrella term for many types of public-private partnerships that finance sustainable energy projects, the IRA contains specific requirements for Green Banks to be able to receive funding. Many states already have established some form of Green Bank, but some are still creating theirs or are still working to meet the new Green Bank requirements in the IRA.

Using Other Federal Funding Sources

In some cases, eligible entities will be able to further supplement Direct Pay funding by using other sources of funding in the IRA (for example, using grant funding for rural electric co-ops) or using funding from other federal programs such as funding in the Infrastructure Investment and Jobs Act or remaining American Rescue Plan funding.

GOING BEYOND THE WORKER PROTECTION REQUIREMENTS IN THE IRA

State funding and state technical assistance programs offer an opportunity to support community uptake of Direct Pay, go beyond the IRA labor requirements, and impose additional protections as a condition of receiving state funds. For example, a state revolving fund to support renewable energy programs could require that programs that receive the state matching funds use union labor. Similarly, state funding could be contingent on the use of pre-hire agreements like local hire programs, Project Labor Agreements (PLAs), Community Workforce Agreements (CWAs), and Community Benefits Agreements (CBAs). It is critical that any state incentives or requirements include strong community input and strong enforcement mechanisms. For more information, please see the CPCC's Guide to IRA Worker Protection Requirements and FAQs on How to Protect Direct Pay Project Workers.

States have a critical role to play in supporting workforce development efforts to build the diverse skilled workforce needed to fully embrace a green energy economy. In addition to the jobs created by the IRA and the growth in green energy infrastructure, more than 1.7 million workers are expected to retire over the next decade. Black, Latino, Native, and Asian individuals, and women are dramatically underrepresented in these growing fields, and state agencies must help build inclusive and equitable workforce development programs. The National Skills Coalition has published a report with recommendations for states in building a just workforce development plan.

TECHNICAL ASSISTANCE AND COORDINATION

States can maximize the number of eligible entities that can access Direct Pay by coordinating technical assistance programs. Creating programs that will qualify for the Direct Pay provisions often requires specialized planning, including conducting an energy audit, creating an interconnection agreement with a utility, and more. Many smaller nonprofit organizations, local governments, and communities that have been systematically excluded, like low-income communities and communities of color, will need help.

TECHNICAL ASSISTANCE

State governments can reduce barriers by funding technical assistance that could include:

- **Public information campaigns about the opportunity**
- **Free energy audits**
- **Hands-on support in planning projects**
- **Support in creating interconnection agreements**
- **Help finding reputable high-road union contractors**
- **Support in completing pre-filing paperwork and IRS documentation. By definition, eligible entities do not usually file complex taxes with the IRS and may lack information and experience in navigating the process.**

Some states have established technical assistance programs to support their state's access to IRA funds. For example, Washington established a statewide Building Energy Upgrade Navigator Program to support building owners in accessing electrification and energy efficiency services, with specific priority for low-income households, vulnerable populations, and overburdened communities. Washington also appropriated $2.5 million to support activities related to securing federal funds, including funding to help community-based organizations, local governments, and ports in overburdened communities apply for financial resources.

State-funded technical assistance programs can help increase equity with implementation efforts. Communities of color that have experienced high levels of contamination, communities transitioning away from extractive industries, tribal governments, rural communities, and other communities facing systemic exclusion are more likely to struggle to secure the up-front capital necessary to complete a Direct Pay-eligible project. State-funded technical assistance programs targeted to communities that need them most can ensure that all communities have equitable access to the benefits of the Direct Pay tax credits, including cleaner air and water, new green energy jobs, and lower energy costs.

State Direct Pay Coordination Program

Centralizing efforts within a state-run program or with a cross-agency coordinator can help maximize Direct Pay programs that would actively identify possible Direct Pay projects and build them using the state as the eligible entity. A state entity could actively search out Direct Pay-eligible opportunities within communities and build the projects directly (for example, put solar panels on all the schools in a local school district, perform energy retrofits on nonprofit-owned affordable housing units, or build utility-scale solar farms on Brownfield land). If the state retained ownership of the energy-generating facility, the state should claim the credit directly and lift the burden of paperwork from the smaller eligible entity. If the smaller entity plans to retain ownership of the energy-generating facility, the state could still carry out the project and receive funding by creating a side agreement with the eligible entity to transfer the credit to the state in exchange for the state completing the process.

Either of these models would streamline the need for many smaller governments and nonprofit organizations to take on the administrative burdens of designing and building eligible programs and navigating the process to receive the tax credit. These types of programs would be embedded within a relevant state agency such as a state department of energy and would need to work closely with local communities to identify projects that reflect community needs, desires, and priorities. This type of approach requires a larger commitment from state champions, but it could significantly increase the speed at which projects could be implemented, reduce administrative burdens on other eligible entities, and allow the state to prioritize projects that serve historically excluded communities.

FURTHER RESOURCES:

The **Congressional Progressive Caucus Center** will provide regular updates and further resources on Direct Pay. You can **sign up for CPCC updates**, including invitations to webinars, technical assistance to help your community get Direct Pay funds, resources to build support for Direct Pay projects, and more. **You can also find additional materials, like FAQs on Direct Pay, on the CPCC's website**. You can also request technical assistance on a Direct Pay project through the CPCC's website by filling out **our technical assistance intake form**.

The **State Innovation Exchange (SiX)** exists to advance a bold, people-centered policy vision in every state in this nation by helping vision-aligned state legislators succeed after they are elected. If you are working to strengthen our democracy, fight for working families, advance reproductive freedom, defend civil rights and liberties, or protect the environment, **reach out to helpdesk@stateinnovation.org** to learn more about SiX's tailored policy, communications, and strategy support and how to join a network of like-minded state legislators from across the country.

For a constantly updated roundup of resources on the Inflation Reduction Act, Direct Pay, and equitable implementation strategies, please visit the **Direct Pay master resources list here.**

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