Congress of the United States

Washington, DC 20515

September 20, 2024

The Honorable Janet Yellen
Secretary
U.S Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

The Honorable Daniel Werfel
Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, DC 20224

The Honorable Michael Regan
Administrator
U.S Environmental Protection Agency
1200 Pennsylvania Avenue, NW
Washington, DC 20460

Dear Secretary Yellen, Commissioner Werfel, and Administrator Regan:

We write to you today regarding the 45Q tax credit, a credit designed to encourage carbon capture and sequestration (CCS) projects. The IRS is expected to release updated guidelines about the tax credit later this year, and the Department of Treasury has estimated that the 45Q tax credit could cost taxpayers up to $30.3 billion over the next ten years.[1] To ensure actual carbon sequestration takes place, we urge your agencies to develop a set of strong guardrails for the 45Q tax credit.

The 45Q tax credit, commonly referred to as the federal carbon sequestration tax credit, can be claimed by "qualified taxpayers for every metric ton of carbon oxide captured and sequestered that would have otherwise been released into the atmosphere."[2] The 45Q credit was initially designed to incentivize investment in CCS and emission reductions. However, the credit has been primarily used to "increase oil production from aging wells, canceling out most of the emissions reduction benefit."[3] Nevertheless, in 2018, Congress expanded the credit to cover carbon dioxide and carbon monoxide emissions and allow companies to claim the credit for 12 years after a facility with carbon capture equipment was placed in service.[4] Then, in 2022, the *Inflation Reduction Act* (IRA) changed "the base credit rates and definition of qualified facilities," allowing more entities to claim the credit and receive more money per ton of carbon. [5]

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[1] Department of Treasury Office of Tax Analysis, "Tax Expenditure Estimates FY 2023," March 6, 2023, https://home.treasury.gov/system/files/131/Tax-Expenditures-FY2024-update.pdf.

[2] Taxpayers for Common Sense, "Hot Air and High Costs: The Carbon Capture and Sequestration 45Q Credit," February 14, 2023, https://www.taxpayer.net/energy-natural-resources/hot-air-and-high-costs-the-carbon-capture-and-sequestration-credit-45q/.

[3] *Id.*

[4] 86 Federal Register 4728.

[5] CRS, "The Section 45Q Tax Credit for Carbon Sequestration," August 25, 2023, Angela C. Jones and Donald J. Marples, https://crsreports.congress.gov/product/pdf/IF/IF11455; Inflation Reduction Act of 2022, Public Law 117-169.

The IRA also significantly increased the base credit if qualified taxpayers adhered to prevailing wage and apprenticeship requirements.[6]

The 45Q credit has been plagued by problems. In 2020, the Treasury Inspector General for Tax Administration (TIGTA) released a report, which analyzed 99.9% of total credits claimed from 2010 to 2019, that found that *87%* of tax credit claims did not comply with the EPA's monitoring, reporting, and verification requirements for carbon sequestration.[7] In other words, close to *$900 million dollars* in tax credits were awarded to taxpayers who did not meet the federal government's requirements.[8] Additionally, the report found that IRS examiners are not required to coordinate with EPA personnel to confirm the amount of carbon sequestered by claimants and that there was no agreement between the agencies that the IRS inform the EPA of basic information about the credit, including claimants, volume of carbon dioxide sequestered, and dollars claimed.[9]

These problems have been further exacerbated by insufficient verification and reporting requirements for taxpayers. Currently, the IRS does not require every taxpayer to submit independent or third-party verification of their carbon sequestration amounts, allowing for self-certification in many instances.[10] There are also no requirements for taxpayers to keep records of their carbon sequestration efforts after the EPA's mandatory 3-year record-keeping threshold, despite taxpayers' eligibility for the credit 12 years after placing a facility in service.[11] The absence of robust requirements has severely hindered the effectiveness of 45Q.

The IRS and EPA must work together to implement basic guardrails for the 45Q tax credit. First, the IRS should mandate independent, third-party verification of carbon sequestration, including for any leaks discovered, for entities to claim the 45Q credit. The reporting requirements for the 45Q credit could draw from other established standards where appropriate.[12] Second, the IRS and EPA must improve coordination to effectively monitor the 45Q tax credit. The agencies should enter into a memorandum of understanding to more effectively share basic data about the credit's implementation, including claimants, volumes of carbon oxides, and tax credit amounts claimed. Finally, the IRS should require more stringent record-keeping requirements and establish a 12-year recapture period for the 45Q credit. For

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[6] CRS, "The Section 45Q Tax Credit for Carbon Sequestration," August 25, 2023, Angela C. Jones and Donald J. Marples, https://crsreports.congress.gov/product/pdf/IF/IF11455; Evergreen Collaborative, "Public Money is Funding Carbon Sequestration. Here's How IRS Must Demand Oversight.," June 6, 2024, https://collaborative.evergreenaction.com/memos/public-money-is-funding-carbon-sequestration-irs-must-demand-oversight-9?utm_source=policy&utm_medium=referral&utm_campaign=ira.

[7] Letter from Department of Treasury Inspector General for Tax Administration to Senator Menendez, April 15, 2020, https://web.archive.org/web/20240528163114/https://www.menendez.senate.gov/imo/media/doc/TIGTA%20IRC%2045Q%20Response%20Letter%20FINAL%2004-15-2020.pdf.

[8] *Id.*

[9] *Id.*

[10] Evergreen Collaborative, "Public Money is Funding Carbon Sequestration. Here's How IRS Must Demand Oversight.," June 6, 2024, https://collaborative.evergreenaction.com/memos/public-money-is-funding-carbon-sequestration-irs-must-demand-oversight-9?utm_source=policy&utm_medium=referral&utm_campaign=ira.

[11] *Id.*

[12] Where possible, the EPA should engage in oversight and verification of carbon sequestration as well (e.g., pursuant to subpart RR). California Air Resources Board, "Mandatory GHG Reporting - Verification," https://ww2.arb.ca.gov/verification.

every year that a taxpayer qualifies for the credit after placing a facility into use, the taxpayer should be required to maintain meticulous records about their carbon sequestration amounts.[13]

We urge you to consider these guardrails as you prepare updated guidelines for the 45Q tax credit to ensure that the credit is aiding in actual carbon sequestration and emissions reductions and that recipients of the credit are not using loopholes to undermine the intent of the law. To that end, we ask that your agencies provide a briefing on these requests by October 4, 2024. Thank you for your attention to this important matter.

Sincerely,

Elizabeth Warren
United States Senator

Ro Khanna
Member of Congress

Angus S. King, Jr.
United States Senator

Alma S. Adams, Ph.D.
Member of Congress

Jan Schakowsky
Member of Congress

Pramila Jayapal
Member of Congress

[13] Eligibility for the credit is reduced to a 5-year period after a facility is placed in service if transferred. CRS, "The Section 45Q Tax Credit for Carbon Sequestration," August 25, 2023, Angela C. Jones and Donald J. Marples, https://crsreports.congress.gov/product/pdf/IF/IF11455.