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November 19, 2019

The Honorable J. Russell George
Treasury Inspector General for Tax Administration
1401 H Street NW, Suite 469
Washington, DC 20005

Dear Mr. George:

I write today in order to raise a number of concerns about the implementation of the tax credit for carbon oxide sequestration (45Q tax credit). Congress intended this tax credit to support permanent, secure geologic storage of carbon oxides that would aid in efforts to reduce the effects of climate change. Publicly available data suggests that the vast majority of the 45Q tax credits claimed have come absent the required monitoring, reporting, and verification systems that ensure the safe disposal of captured carbon, in clear contravention of current law and guidance.

I raised these concerns through recent written correspondence with the Internal Revenue Service (IRS). Their response, attached to this letter, fails to provide justification for the discrepancies between the tax credits claimed and the apparent failure of these claimants to comply with monitoring, reporting, and verification requirements. Given this, I request that your office undertake an investigation into whether 45Q tax credit claimants are complying with the law, and whether the IRS is properly enforcing the law.

In interim guidance issued through Notice 2009-83 in 2009, the IRS stated “In order to qualify for the § 45Q credit, a taxpayer must either physically or contractually dispose of captured CO₂ in secure geological storage using adequate security measures as provided by the Secretary in regulations.”¹ That notice established interim procedures to demonstrate secure geologic storage while the Environmental Protection Agency (EPA) worked to issue a final set of standards.

EPA’s standards were ultimately finalized in December of 2010, through the Greenhouse Gas Reporting Requirement under Subpart RR, Geologic Sequestration of Carbon Dioxide². The application of these requirements to claimants of the 45Q tax credit was further emphasized when the IRS published its December 2013 Oil and Gas Handbook. The handbook includes the following references:

¹ IRS Notice 2009-83. <https://www.irs.gov/pub/irs-drop/n-09-83.pdf>

² EPA, Subpart RR – Geologic Sequestration of Carbon Dioxide. <https://www.epa.gov/ghgreporting/subpart-rr-geologic-sequestration-carbon-dioxide>.

- “IRC 45Q and Notice 2009-83 state that a taxpayer claiming the credit must comply with evolving rules of the U.S. Environmental Protection Agency (EPA) regarding the sequestration of CO₂ and reporting of CO₂ volumes measured at the source of capture and verified at the point of disposal or injection.”
- “EPA promulgated final rules regarding the reporting of both CO₂ emissions and CO₂ use (including sequestration) for years after 2010. Subpart RR – Geologic Sequestration of Carbon Dioxide is applicable to the IRC 45Q credit.”
- “The Preamble to EPA’s final rule states in plain language that, under the final rule, operators of facilities that are sequestering CO₂ in geologic storage must comply with Subpart RR regardless of whether the CO₂ is currently used as a tertiary injectant in an EOR project. EPA’s preamble also states that taxpayers claiming the 45Q tax credit after 2010 must follow Subpart RR’s “MRV procedures”. MRV stands for Monitor, Report and Verify. The MRV procedures require the operator to submit an MRV plan to the EPA for its approval, and to annually report CO₂ volumes, including amounts sequestered, pursuant to the plan. Examiners should obtain a copy of these documents.”
- “Tax credits claimed by the taxpayer in years after 2010 should be reconciled with annual volumes reported by the operator of the facility to the EPA under its subpart RR rules.”³

Both the EPA and the IRS have made it abundantly clear that eligibility for the 45Q tax credit is contingent upon compliance with EPA’s requirements under Subpart RR, including the creation of an MRV regime designed to ensure that carbon is sequestered securely.

Yet based on a review of publicly available information, it appears that millions of dollars of tax credits have been claimed by companies that are not complying with EPA’s MRV standards. According to IRS’s response to my inquiry, 62,740,171 metric tons of carbon dioxide has been reported for purposes of claiming the 45Q tax credit.

Given that claimants of the 45Q tax credit are subject to EPA’s MRV procedures, EPA’s greenhouse gas reporting database should reflect at least 62.7 million metric tons of carbon that have been permanently stored. Yet just 16,710,550 metric tons of carbon have been sequestered in accordance with EPA’s standard, according to EPA’s Facility Level Information on Greenhouse Gas Tool (FLIGHT)—just a fraction of the sequestered carbon for which tax credits have been issued⁴. The earliest entry into this database is from 2016, five years after the EPA MRV process was established.

In its response to my correspondence, the IRS failed to provide an adequate explanation for this discrepancy. The IRS states that “Taxpayers have claimed a credit under Section 45Q with the IRS beginning in 2008. In contrast, the Subpart RR requirements were finalized in 2010, and 2016 was the first year that any facility reported data to EPA under Subpart RR.” This confirms an extended time period in which taxpayers were claiming the 45Q credit without complying

³ IRS, Section 1: Oil and Gas Handbook. https://www.irs.gov/irm/part4/irm_04-041-001#idm139662020024880.

⁴ EPA Facility Level Information on Greenhouse Gases Tool. Accessed 11/19/19. <https://ghgdata.epa.gov/ghgp/main.do#>

with applicable MRV standards, but fails to provide any rationale for how these actions would be permissible under law.

It appears that following the issuance of the EPA regulations, a significant amount of tax credits were improperly claimed by filers who failed to comply with the clear standards of the law. Fraudulent claims on these credits have the potential to seriously undermine both public confidence in the potential of carbon capture technology, and the efforts of those that are acting in compliance with the IRS and EPA's requirements.

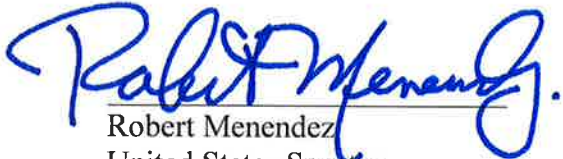
Given this, I request that the Inspector General's office undertake an investigation into the discrepancies between the amount of 45Q tax credits that have been claimed, and the amount of sequestered carbon reported to the EPA. Specifically, I request that you investigate the following matters:

- 1) What is the reason for the discrepancy between the amount of sequestered carbon cited by claimants of the 45Q tax credit versus the amount of sequestered carbon reported to the EPA under Subpart RR?
- 2) What is the value of 45Q tax credits claimed for sequestered carbon that was not in compliance with the EPA's Subpart RR monitoring, reporting, and verification requirements?
- 3) What enforcement actions should the IRS take to ensure that in the future, all claimants of the 45Q tax credit are complying with the required monitoring, reporting, and verification requirements?
- 4) What actions should the IRS take against previous claimants of the 45Q tax credit that have not complied with the required EPA monitoring, reporting, and verification requirements?
- 5) In its response to my letter, the IRS notes there may be a temporary discrepancy between the amount of tax credits claimed and the amount reported to the EPA due to ongoing audits. What percentage of the current claimants of the 45Q tax credit are currently under an audit that may have created such a discrepancy?
- 6) What is the IRS process for coordinating with EPA when it assesses a 45Q claimant's eligibility for the tax credit? Should that process be altered to in any manner to ensure full compliance with the law?

I urge you to closely examine these discrepancies, and to ensure that the 45Q tax credit is only provided to taxpayers that adhere to existing requirements and ensure permanent, secure storage of all sequestered carbon. Without these compliance measures, there can be no assurances that the 45Q tax credit is actually preventing carbon from being released into our atmosphere.

Thank you for your prompt attention to this critical matter.

Sincerely,


Robert Menendez
United States Senator