TAXPAYERS for COMMON SENSE

5 FAST FACTS

about

Oversight of the 45Q Tax Credit

The 45Q tax credit for carbon sequestration was first introduced in 2008 under the Energy Improvement and Extension Act to incentivize carbon capture investments. It was significantly expanded in 2018 through the Bipartisan Budget Act, which removed the cap on the total amount of carbon eligible for the credit, and in 2022 through the Inflation Reduction Act (IRA), which further increased the credit amounts.

Current IRS regulations for the 45Q tax credit, issued in 2021, have significant oversight gaps that may leave the 45Q credit vulnerable to fraud and abuse. The current rules do not sufficiently ensure that facilities have sequestered the amount of carbon they claim for the credit or that the sequestered carbon remains underground. As the IRS works on a proposed rule to implement changes directed by the IRA, the agency has an opportunity to address these oversight gaps.

1. INADEQUATE EPA MONITORING, VERIFICATION AND REPORTING REQUIREMENTS

Facilities claiming the 45Q credit for geological sequestration are required to report to the Environmental Protection Agency (EPA) under Subpart RR of the Greenhouse Gas Reporting Program. Subpart RR requires facilities to have EPA-approved monitoring, reporting, and verification (MRV) plans, which only describe how facilities *intend* to monitor leaks. However, the EPA does not prescribe specific monitoring strategies or technologies for these plans, leaving companies to set their own standards. There are also no explicit requirements for the timing of monitoring activities or for the onsite verification of data submitted under Subpart RR.

2. LACK OF TRANSPARENCY AND LEAKAGE REPORTING IN ISO STANDARDS

Facilities claiming 45Q credits for enhanced oil recovery (EOR) can opt to comply with either EPA Subpart RR or the International Organization for Standardization standard (CSA/ANSI ISO 27916:19). The ISO standard does not mandate reporting of leakage information, which raises concerns, as leakage from EOR projects can occur over decades. Additionally, the IRS does not require EOR operators using the ISO standard to make their reports publicly available.

3. PROBLEMATIC SELF-CERTIFICATION AND LACK OF ONSITE VERIFICATION

The IRS allows operators complying with Subpart RR to self-certify the volumes of carbon dioxide they report for claiming 45Q tax credits. This self-certification may not reflect actual sequestered volumes. While Subpart RR data is publicly available, it does not provide enough information to verify the total amount eligible for the 45Q credit, as it only requires reporting the aggregate volume of sequestered carbon, which could include ineligible sources like naturally occurring reservoirs. Neither the EPA nor the IRS perform onsite verification, which raises further concerns about the reliability of the data used to claim these tax credits. More robust oversight, including third-party verification, is needed to ensure the accuracy and credibility of reported data.

4. INSUFFICIENT RECORD-KEEPING AND RECAPTURE PERIOD

Although taxpayers can claim 45Q tax credits for up to 12 years, both the IRS and EPA only require facilities to retain records for three years. The IRS also set the recapture period—the timeframe during which the IRS can claw back 45Q credits if stored or injected carbon gets leaked—at just three years. This discrepancy complicates efforts to manage long-term liabilities associated with carbon storage.

5. HISTORICAL INSTANCES OF FRAUD AND ABUSE

A 2020 investigation by the Treasury Inspector General for Tax Administration revealed significant fraud in the 45Q tax credit program, with approximately $894 million in credits claimed without complying with EPA reporting requirements. These facilities claimed the credits before obtaining EPA-approved MRV plans. The investigation exposed systemic oversight weaknesses, highlighting the need for stronger safeguards to prevent fraudulent claims. While the 2021 rule clarified some reporting and documentation requirements, the regulatory framework still has significant gaps that leave the 45Q program vulnerable to ongoing abuse.