Leveraging IRA leadership

The US Inflation Reduction Act (IRA) is a profound step in advancing climate leadership, despite coming from a deeply divided nation. Now is the time to show that the landmark policy could lead to progress and profits where the country is not divided, such as overseas engagement and climate leadership, argue David Williams and Daniel Kammen of the University of California, Berkeley.

The US has much to do if it is to usher in a clean energy revolution. But even with this success, the nation must also think globally in terms of acceleration of carbon neutrality goals for job creation, to address energy inequality and safeguard the planet. We need to act globally, or domestic progress will mean very little.

We can achieve these objectives by extending proven tax incentive tools to unlock the massive investment necessary across Africa and other industrializing economies. This will help to build markets and create jobs for the clean energy sector in the US. Developers will have an entirely new pool of sophisticated investors and the capital necessary to match the scale of the climate challenges.

The number of unelectrified Africans has remained nearly unchanged at over 600 million for over a decade, despite efforts aimed at achieving the UN Sustainable Development Goal (SDG7) to provide global energy access by 2030.

At COP26 in Glasgow in Nov. 2021, the international community made a commitment of $100 billion to industrializing nations. This is an order of magnitude smaller than what is needed on an annual, ongoing basis to build a decarbonized, affordable and resilient energy future. Clean energy is now cheaper to build and simpler to operate than existing fossil fuel projects. Africa needs massive and sustained financing for new, bankable projects.

Photo: USAID

USAid Administrator Samantha Power met with Yemi Osinbajo, vice president of Nigeria, in September to discuss the African country's energy transition plans, and potential energy sector partnerships with the United States. As well as supporting clean energy, the Inflation Reduction Act can also boost US climate leadership abroad, argue experts from University of California, Berkeley.

Electrifying Africa

The Africa electrification story is complex because "bankable" projects are dependent not only on designing good projects but also on the twin constraints of sustaining capital from investors and then navigating complex local regulatory issues. Sub-Saharan African projects are often held up because of a lack of "first-loss capital" (high risk) funding that leverages bank and central government investments.

There is, however, a simple solution that provides risk-tolerant first-loss capital at scale and leverages hundreds of billions in a global renewables industry. This solution is to extend the IRA to specific projects in Africa. This would strengthen investment by US companies and support individual country's geopolitical goals. This tax credit would afford the same incentives internationally that already include investments in solar, wind, geothermal, sustainable hydropower, energy efficiency upgrades, and transmission and distribution projects.

Tax incentives work

Tax incentive investing works. The US Investment Tax Credit is responsible for the dramatic successes of solar across the US since its launch in the Energy Policy Act of 2005. The program has been highly popular and an economic engine creating over 230,000 jobs in every state with an annual private investment of over $30 billion all while making renewable energy more affordable than conventional energy sources. The program has challenges but is resoundingly successful by relying on private companies to make good investments.

The economic needs for African energy are tremendous and aid is simply not enough. At COP26, US and European partners committed $7.5 billion in aid for the ailing South African energy sector. Nigeria has publicly stated a request for a comparable amount. These investments are critically needed to upgrade or build grid transmission assets, to invest in new clean energy projects, reduce methane fugitive emissions, invest in energy access, and launch electric vehicle markets.

$400 billion are needed beyond business as usual for each African country to achieve a clean energy transition. That is almost a trillion dollars of investment opportunity for US companies to support just energy transitions in just two nations. Rewarding US companies for investing in commercial clean energy projects in Africa will enable a transition that cannot be achieved with public sector funds alone.

This can be launched quickly and can be in place for the COP27 meeting in Egypt in November. The Institute on Taxation and Economic Policy found that at least 55 of the largest corporations in the US paid no federal corporate income taxes on their 2020 profits. Over $8 billion in avoided tax a year is in complex offshore structures. The tax incentive we propose corrects this by providing the private sector a clear means to back up their public statements of commitment to a just energy transition via direct investments in the neediest and fastest growing markets.

Modest changes

This "simple" solution requires only a modest change to the US investment Tax Credit program to extend eligibility to certain international projects. The US direct aid and web of supporting wraparound services certainly make a difference but are not enough.

Extending proven US policy would be a significant catalyst for capital directed to industrializing energy markets. In the past year, we have seen multibillion-dollar investments in solar, storage, and electric vehicles in Angola, plans in Kenya to move from a 4 GW national grid to 100 GW by mid-century, and both Nigeria and South Africa commit to going carbon-free if investment flows to solar, wind, energy storage, electrified transportation, and green hydrogen. The markets are there, the time is now, and what is most needed is a means to move capital.

The climate-vulnerable are susceptible to the impacts of climate change and are the most affected by weaponizing energy. This is a unique moment where political will can bring incremental tax code changes that democratize, decarbonizes, and decreases the conflict costs of energy around the world. This just might be the match that lights renewable solutions for the rest of the world. pv

David Williams and Daniel Kammen

The US Tax Investment Credit has helped create

230,000

jobs

About the authors

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