

Treasury and IRS Issue Additional Domestic Content Guidance Under IRA and New Elective Safe Harbor

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On May 16, the Treasury Department (Treasury) and the Internal Revenue Service (IRS) issued [Notice 2024-41](#), which modifies [Notice 2023-38](#) (Prior Guidance) by expanding the list of Applicable Projects (defined below) to include hydropower and pumped hydropower storage facilities and provides a new safe harbor (New Elective Safe Harbor) that taxpayers may elect to use to calculate the domestic cost of Manufactured Products (defined below) and Manufactured Product Components (defined below) within a Project. Under the [Inflation Reduction Act of 2022](#) (IRA), projects that satisfy applicable “Buy American” requirements (the domestic content requirement) qualify for enhanced credit amounts for several clean energy tax credits, including investment tax credits under Sections 48 and 48E (ITC) and production tax credits under Sections 45 and 45Y (PTC).

Treasury and the IRS intend to include the rules in the Prior Guidance, as modified by the notice, in forthcoming proposed regulations concerning domestic content, which will apply to taxable years ending after May 12, 2023. Taxpayers may rely on the Prior Guidance, as modified by the notice, with respect to the domestic content requirements for any qualified facility, energy project, or energy storage technology (each, an Applicable Project) the construction of which begins before the date that is 90 days after the date of publication of the forthcoming proposed regulations in the *Federal Register*. Taxpayers may rely on the New Elective Safe Harbor for any Applicable Project the construction of which begins before the date that is 90 days after any future modification, update, or withdrawal of the New Elective Safe Harbor.

Overview

In general, the domestic content requirement applies to any steel, iron, or item produced as part of a manufacturing process (a Manufactured Product) that is a component of an Applicable Project (an Applicable Project Component).

The domestic content requirement with respect to steel or iron (Steel or Iron Requirement) is met if, consistent with 49 CFR § 661.5(b) and (c), all manufacturing processes with respect to any steel or iron items that are Applicable Project Components take place in the U.S., except metallurgical processes involving refinement of steel additives.

The domestic content requirement with respect to manufactured products (Manufactured Products Requirement) is met if all Applicable Project Components that are Manufactured Products are produced in the U.S. or are deemed to be produced in the U.S. All Applicable Project Components that are Manufactured Products are deemed to be produced in the U.S. if the Adjusted Percentage Rule (described below) is satisfied.

Steel or Iron Requirement Under Prior Guidance

The Steel or Iron Requirement applies to Applicable Project Components that are construction materials made primarily of steel or iron and are structural in function. The Steel or Iron Requirement does not apply to steel or iron used in articles, materials, or supplies, whether manufactured or unmanufactured, that are directly incorporated into an Applicable Project Component that is a Manufactured Product (Manufactured Product Components) or subcomponents of Manufactured Product Components. The Prior Guidance included a table that categorized certain items as either subject to the Steel or Iron Requirement or Manufactured Product Requirement (the Safe Harbor Classifications).

- The Prior Guidance specified that the Safe Harbor Classifications may not be an exhaustive set of all components for a Project. Accordingly, taxpayers needed to consider whether any items made primarily of steel or iron that were not specifically listed could be treated as an Applicable Project Component that is structural in function (as opposed to an Applicable Project Component that is not structural in function or a Manufactured Product Component). Given the binary nature of the Steel or Iron Requirement, the uncertainty related to those determinations has made it challenging for taxpayers (and financing parties) to be confident the Steel or Iron Requirement has been satisfied.

Adjusted Percentage Rule Under Prior Guidance

The Domestic Cost Percentage for an Applicable Project is equal to the percentage produced by dividing the Domestic Manufactured Products and Components Cost by the Total Manufactured Products Cost. If the Domestic Cost Percentage for an Applicable Project equals or exceeds the adjusted percentage that applies to the Applicable Project, then the Applicable Project satisfies the Adjusted Percentage Rule. For most projects under the rules now in effect, the adjusted percentage is 40%.

The Domestic Manufactured Products and Components Cost is based on the sum of (1) the direct materials and direct labor costs incurred by U.S. Manufactured Product manufacturers to produce each U.S. Manufactured Product (products that are manufactured in the U.S. using only U.S. Components) and (2) the direct materials and direct labor costs incurred by non-U.S. Manufactured Product manufacturers to produce or acquire U.S. Components. The relevant direct costs are determined by reference to Treasury Regulation Section 263A-1(e)(2)(i). The Total Manufactured Products Cost for an Applicable Project is the sum of the costs of each Applicable Project Component that is a Manufactured Product.

- As expected when the Prior Guidance was released, the focus on manufacturers' direct costs under Section 263A made compliance with the domestic content requirement extremely difficult. To satisfy the requirement, taxpayers needed to gather cost data from multiple suppliers and manufacturers (both foreign and domestic), many of whom have been unable or unwilling to provide such data. As a result, it has been very difficult to finance any project assuming that the domestic content bonus will apply.

Updates to Prior Guidance Safe Harbor

For purposes of classifying certain Applicable Project Components as steel or iron or as Manufactured Products, and for identifying certain Manufactured Product Components, Table 2 of the Prior Guidance provided a safe harbor for certain components of utility scale solar projects, land-based and offshore wind facilities, and battery energy storage facilities. The notice updates the Safe Harbor Classifications to add Applicable Project Components and Manufactured Product Components of hydropower facilities and pumped hydropower storage facilities. It also expands the applicability of the solar category by modifying the terminology to replace “Utility-scale photovoltaic system” with “Ground-mount and rooftop photovoltaic systems.”

- Notably, the updates to the Safe Harbor Classifications once again leave out renewable natural gas projects. Developers and investors will likely continue to struggle to be comfortable that the bonus applies to such projects.
- The updates also fail to address project substation equipment, such as generator step-up transformers (except in the case of hydropower or pumped hydropower storage).

New Elective Safe Harbor

The notice sets forth the New Elective Safe Harbor in Table 1, which applies to both the Steel or Iron Requirement and Manufactured Products Requirement. The New Elective Safe Harbor provides for the classification of identified Applicable Project Components (as Steel or Iron or Manufactured Products) and the associated cost percentages for each of the identified Manufactured Products and Manufactured Product Components, consistent with those identified in the updated Table 2 from the Prior Guidance. Taxpayers that elect to use the New Elective Safe Harbor must use the list as the exclusive and exhaustive set of all Applicable Project Components and Manufactured Product Components for a project.

- By treating Table 1 as the exclusive set of Applicable Project Components, taxpayers can rule out the possibility that any items not included in Table 1 could be subject to the Steel or Iron Requirement.
- The notice acknowledges that the requirement to gather cost data from multiple suppliers and manufacturers, including foreign manufacturers, may present challenges for substantiation and verification. The New Elective Safe Harbor allows taxpayers to satisfy the Adjusted Percentage Rule without obtaining manufacturer direct cost data.
- The notice indicates that the cost percentage information was obtained from the Department of Energy (DOE) for purposes of calculating the Domestic Cost Percentage to satisfy the Adjusted Percentage Rule. The DOE obtained the cost data from a variety of sources, including datasets of system characteristics, price indices, U.S. survey data from the government and private sector, public filings from corporations, and comprehensive interviews of manufacturers, installers, developers, and owners of the representative technologies.

To apply the New Elective Safe Harbor, a taxpayer adds up the assigned cost percentages from Table 1 for each U.S. Component and U.S. Manufactured Product of the Applicable Project, which equals the Domestic Cost Percentage. Any Manufactured Product or Manufactured Product Component listed in Table 1 that is not in the

Applicable Project must be assigned a zero value (with no changes to the assigned cost percentage for the other items), and any Manufactured Product or Manufactured Product Component not listed in Table 1 must be disregarded. Taxpayers must affirmatively elect to rely on the New Elective Safe Harbor by providing notice to the IRS on the Domestic Content Certification Statement required by the Prior Guidance.

The notice includes a formula to address scenarios where a taxpayer sources the same type of Manufactured Product or Manufactured Product Component from both foreign and domestic sources (a Mixed Source Item). For Mixed Source Items with a nameplate capacity, the formula is based on nameplate capacity produced in the U.S. vs. total nameplate capacity. For Mixed Source Items without a nameplate capacity, the formula is based on the nameplate capacities of the associated Applicable Project Components with which the Mixed Source Item is directly integrated (e.g., the nameplate capacity of associated PV modules for items in the Solar PV portion of Table 1).

- While the New Elective Safe Harbor removes the requirement to obtain direct cost information, taxpayers must still obtain information from suppliers and manufacturers in order to determine which parts of their project constitute a U.S. Manufactured Product or a U.S. Component.
- Table 1 includes a line item for “Production”, which refers to the production cost of the relevant Manufactured Product. Production can be included in the Domestic Cost Percentage only if all the Manufactured Product Components of a Manufactured Product are produced in the U.S.

Conclusion

The notice provides a long-awaited alternative path to meeting the domestic content requirements, which should allow some projects to qualify for the domestic content bonus. However, the notice leaves some notable gaps, particularly regarding equipment not included in the modified Table 2 from the Prior Guidance or the new Table 1. The notice will also likely solidify suppliers’ resistance to providing cost information, as it is no longer a taxpayer’s only means of qualifying for the bonus.

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