

IRS Safe Harbor Eases Path for Domestic Content Bonus Tax Credits

IRS Notice 2024-41 provides taxpayers with a clearer path toward qualifying for domestic content bonus tax credits through a new elective safe harbor.

Key Points:

- The new guidance fixes a number of challenges that were stopping project owners from claiming domestic content bonus tax credits.
- A new and fairly simple elective safe harbor should enable many projects to qualify for domestic content bonus tax credits by adding up costs from a table provided by the IRS.
- Qualification using a more complex method is still available under previously issued guidance.

The Inflation Reduction Act of 2022 (the IRA) created bonus tax credits that are intended to incentivize developers to use American-made steel, iron, and manufactured components to build their projects. On May 16, 2024, the IRS released Notice 2024-41 (the New Notice), which modifies guidance on qualifying for domestic content bonus tax credits for renewable energy projects provided in Notice 2023-38 (the Original Notice). The New Notice, together with the Original Notice, explains how to comply with the two principal requirements to qualify for domestic content bonus tax credits (collectively, the Domestic Content Requirement): (i) all steel or iron in a project must be manufactured in the US (the Steel and Iron Requirement); and (ii) a specified percentage of the manufactured products in a project must be US-manufactured (the Adjusted Percentage Test).

Under the Original Notice, project owners were struggling to prove that they satisfied the Domestic Content Requirement, which required them to obtain detailed cost information from their suppliers to support meeting the Adjusted Percentage Test. In contrast, the New Notice does not require supplier cost information. Instead, a project owner may elect to apply a safe harbor (the New Elective Safe Harbor) that allows the project owner to use the classifications of components and cost percentages listed on an IRS table to determine if the project contains domestic content components in sufficient quantities to qualify for bonus tax credits.

In addition to introducing the New Elective Safe Harbor, the New Notice includes specific technical adjustments that expand and modify the guidance included in the Old Notice with respect to the categorization of project components, including by identifying and categorizing applicable project components and manufactured product components of hydropower projects and pumped hydropower storage facilities. These technical adjustments are not addressed in detail in this Client Alert.

Domestic Content Bonus Tax Credits — General Rules

The IRA provides a bonus tax credit for certain projects placed in service in 2023 or later that satisfy the Domestic Content Requirement. If the Domestic Content Requirement is met, projects claiming an investment tax credit (ITC) can claim up to an additional 10% ITC, while projects claiming a production tax credit (PTC) may increase their PTCs by 10%. Retrofitted projects that qualify as newly placed in service for tax purposes may also qualify for these additional tax credits if the new property incorporated into the project satisfies the Domestic Content Requirement.

Under the IRA, the Steel and Iron Requirement is satisfied if any steel or iron that is a component of the project is manufactured in the US (other than metallurgical processes involving refinement of steel additives), and the Adjusted Percentage Test is met if a specified minimum percentage (the Adjusted Percentage) of the direct costs of manufactured products and their constituent components are attributable to US-manufactured products or components. For offshore wind projects, the minimum percentage is 20%, while for onshore wind, battery storage, and solar energy projects that claim the ITC or PTC, the minimum percentage is generally 40%. For projects that will claim the technology neutral credits available for projects beginning construction after 2024, the Adjusted Percentage increases gradually to 55% based on the year the project begins construction.¹

The Original Notice and Its Challenges

Prior to the introduction of the New Elective Safe Harbor, in order to determine whether the Adjusted Percentage Test was met, taxpayers were required to rely on the direct costs of materials and labor that were paid or incurred by the manufacturer of manufactured products, as well as US components incorporated into non-US manufactured products. This approach required gathering data that many manufacturers may have been reluctant to share. In addition, except for iron and steel that was part of a manufactured product, a project owner was required to prove that all components incorporated into the project that were made primarily of iron or steel and were structural in function were made exclusively in the US.

The Original Notice included a list categorizing project components into manufactured products or steel/iron components, depending on the type of renewable energy project. However, the Original Notice was unclear as to whether this list was exhaustive of all components that the IRS would view as included in a project. Accordingly, to qualify for bonus tax credits, taxpayers were required to determine whether a project contained any additional manufactured products or manufactured product components, as well as any additional structural steel and iron applicable project components. While this method of qualifying under the Original Notice remains available, it involves a significant amount of complexity and uncertainty.

New Elective Safe Harbor

By contrast, the New Notice offers taxpayers a much clearer path toward qualification. For purposes of applying the New Elective Safe Harbor, Table 1 of the New Notice (provided at the end of this Client Alert as [Figure 1](#)) constitutes an exclusive and exhaustive list of the project components that are treated as relevant for purposes of satisfying the Domestic Content Requirement. As a result, the New Elective Safe Harbor simplifies the Domestic Content Requirement by specifying which project components are required to be entirely manufactured in the US in order to satisfy the Steel and Iron Requirement and which manufactured products (and their constituent components) are included in the calculation to determine whether the Adjusted Percentage Test has been met. The manufacturing locations of any project components not listed in Figure 1 are not treated as relevant for purposes of satisfying the Domestic Content Requirement under the New Elective Safe Harbor.

Additionally, the New Elective Safe Harbor allows taxpayers to avoid the requirement to obtain direct cost data from their suppliers. Instead, taxpayers can rely on an exhaustive and exclusive list of project components incorporated into photovoltaic solar, onshore wind, and battery storage projects, as well as their classification as either manufactured products or steel/iron products. A copy of that list is included in Figure 1. Because this list is exclusive and exhaustive, project owners should consider the specific makeup of their particular projects before seeking to apply the New Elective Safe Harbor.

Importantly, projects that include components not listed in Figure 1 may still use the Elective Safe Harbor by simply ignoring those unlisted components for purposes of determining compliance with the Adjusted Percentage Test.

Computing the Assigned Cost Percentage

The manufactured products included in Figure 1 are further broken down into manufactured product components, and each manufactured product component is assigned a fixed number representative of the percentage of costs attributable to that manufactured product component in relation to the total cost of manufactured products included in the project (the Assigned Cost Percentage). If a manufactured product component has been manufactured in the US, then the taxpayer is permitted to use the Assigned Cost Percentage to calculate the percentage of manufactured products that are US-manufactured products.

The sum of the Assigned Cost Percentages for manufactured product components that are manufactured in the US must equal at least the Adjusted Percentage to pass the Adjusted Percentage Test. The ability to use a fixed percentage is expected to greatly simplify the process of calculating the Adjusted Percentage. This, in turn, is expected to lead to a significantly easier process for developers looking to monetize domestic content bonus tax credits.

For components that are sourced partially from within the US and partially from abroad, a weighted average formula is applied based on the percentage of the project's nameplate capacity attributable to US-sourced components. In the case of a combined solar PV system and BESS project, the weighted average calculation incorporates an additional specified factor that adjusts the weighting of production between the relative capacities of the PV system and BESS.

Taxpayers that elect to apply the New Elective Safe Harbor can rely solely on the components listed in Figure 1, based on the applicable project category, and allocate costs for each of those components based on the Assigned Cost Percentage. For projects that do not include all components listed in Figure 1, the Assigned Cost Percentage for missing components is subtracted from the total US cost percentage to determine compliance with the Adjusted Percentage Test. The Assigned Cost Percentage applies regardless of the actual cost percentage of such component, and taxpayers that elect to use the New Elective Safe Harbor must use the applicable Assigned Cost Percentage.

How Will the New Elective Safe Harbor Work in Practice?

The New Notice includes a number of useful examples to illustrate how the New Elective Safe Harbor is intended to operate. For example, assume that in an applicable onshore wind project, a taxpayer elects to use the New Elective Safe Harbor. Four applicable project components are identified in Figure 1 for a land-based wind project: wind turbine, wind tower flanges, tower, and steel rebar in the foundation.

The tower and the steel rebar in the foundation are both steel and iron products and are therefore subject to the Steel and Iron Requirement. For purposes of this example, all of the manufacturing processes with respect to the tower and steel rebar in the foundation take place in the US (as necessary to satisfy the Steel and Iron Requirement). The wind turbine and the wind tower flanges are identified as manufactured

products in Figure 1. The wind turbine is made of four manufactured product components — blades, rotor hub, nacelle, and power converter. In this example, the blades and nacelle are manufactured in the US, but the rotor hub and power converter are not. The wind turbine, therefore, is not a US manufactured product under the rules. However, the two manufactured product components that are US components, the blades and nacelle, are identified in Figure 1 as constituting 31.2% and 47.5% of the total costs of manufactured products of a land-based wind facility under the New Elective Safe Harbor. Adding those percentages together, the Domestic Cost Percentage for this project is 78.7%, which exceeds the applicable Adjusted Percentage in 2024 of 40%. Because the Adjusted Percentage Test has been met, it is not necessary to consider whether the wind tower flanges were manufactured in the US.

As the project in this example satisfies the Steel and Iron Requirement and meets the Adjusted Percentage Test, this project meets the Domestic Content Requirement and therefore would be eligible for the domestic content bonus tax credit. Notably, even if this project also included an interconnection transformer and substation, the New Elective Safe Harbor ignores the costs of that equipment entirely because it is not included in Figure 1.

The examples provided in the New Notice illustrate how useful the New Elective Safe Harbor will be, as taxpayers electing to apply the New Elective Safe Harbor will be able to pre-plan and focus their domestic sourcing efforts without having to take into account the manufacturer's actual direct costs. Application of the New Elective Safe Harbor eliminates the risk that inflation or supply chain issues could knock a carefully planned project out of qualifying for the domestic content bonus tax credit. It also allows project owners to more confidently develop mixed foreign and domestic supply strategies to reduce costs.

Certification and Election

In order to claim domestic content bonus tax credits for a project, taxpayers must attach a certification to their tax return for the year that the project is placed in service, and for each subsequent year in which they claim the domestic content bonus tax credits (i.e., each of the following 10 years for PTC projects). This certification must provide that, as of the date the project was placed in service, the Steel and Iron Requirement and the Adjusted Percentage Test were satisfied. Taxpayers that are relying on the New Safe Harbor must include a statement to this effect on their first tax return claiming the domestic content bonus tax credit for the applicable project. Taxpayers are also required to meet general recordkeeping requirements in order to substantiate satisfaction of the Domestic Content Requirement (such recordkeeping requirements have not been significantly modified by the New Notice).

Taxpayer Reliance

Taxpayers are permitted to rely on the Original Notice, as modified by the New Notice, for a project that begins construction prior to the date that is 90 days after the date of forthcoming regulations on the Domestic Content Requirement, and may rely on the New Elective Safe Harbor for a project that begins construction prior to the date that is 90 days after any future modification, update, or withdrawal of the New Elective Safe Harbor.

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Figure 1: IRS Table of Applicable Project Components

(1) SOLAR PV TABLE

Applicable Project Component	Manufactured Product Component	<u>Ground-mount (Tracking)</u>	<u>Ground-mount (Fixed)</u>	<u>Rooftop (MLPE)</u>	<u>Rooftop (String)</u>
PV module	Cells	36.9	49.2	21.5	30.8
	Frame/Backrail	5.3	7.0	3.1	4.4
	Front Glass	3.7	4.9	2.2	3.1
	Encapsulant	2.2	3.0	1.3	1.8
	Backsheet/Backglass	3.7	4.9	2.1	3.1
	Junction Box	1.6	2.2	1.0	1.4
	Edge Seals	0.2	0.2	0.1	0.2
	Pottants	0.2	0.2	0.1	0.2
	Adhesives	0.2	0.2	0.1	0.2
	Bus Ribbons	0.4	0.5	0.2	0.3
	Bypass Diodes	0.4	0.5	0.2	0.3
	Production²	11.5³	15.3³	6.7³	9.6³
Inverter	Printed Circuit Board Assemblies	3.0	4.0	16.0 ⁴	2.5
	Electrical Parts ⁵	1.0	1.3	1.6	1.1
	Climate Control	0.7	0.9	-	0.3
	Enclosure	1.0	1.3	1.6	0.8
	Production	3.3³	4.4³	16.4³	2.9³
PV Tracker or Non-Steel Roof Racking	Torque tube	9.7	-	-	-
	Fasteners	0.4	-	11.1	16.0
	Slew Drive	2.0	-	-	-

	Dampers	0.4	-	-	-
	Motor	3.1	-	-	-
	Controller	0.9	-	-	-
	Rails	2.0	-	8.6	12.3
	Production	6.2³	-	6.1³	8.7³
Steel photovoltaic module racking	-	-	Steel/Iron Product	-	-
Pile or ground screw	-	Steel/Iron Product	Steel/Iron Product	-	-
Steel or iron rebar in foundation	-	Steel/Iron Product	Steel/Iron Product	-	-
Total	-	100	100	100	100

(2) LAND-BASED WIND TABLE

Applicable Project Component	Manufactured Product Component	Value
Wind Turbine	Blades	31.2
	Rotor Hub	9.9
	Nacelle	47.5
	Power Converter	8.9
	Production	0.9³
Wind Tower Flanges	Material ⁶	0.8
	Production	0.8³
Tower	-	Steel/Iron Product
Steel or iron rebar in foundation	-	Steel/Iron Product
Total	-	100

(3) BATTERY ELECTRIC STORAGE SYSTEM (BESS) TABLE

Applicable Project Component	Manufactured Product Component	Grid-scale BESS	Distributed BESS
Battery Pack	Cells	38.0	18.1
	Packaging	3.3	30.1
	Thermal Management System	4.9	9.0
	Battery Management System	5.2	9.0
	Production	21.1³	27.3³
Inverter	Printed Circuit Board Assemblies	1.7	3.8
	Electrical Parts ⁵	0.6	0.4
	Climate Control	0.4	-
	Enclosure	0.6	0.4
	Production	1.9³	1.9³
Battery Container/Housing	Battery Racks and Metal Enclosure	15.8	-
	Production	6.5³	-
Steel or iron rebar in foundation	-	Steel/Iron Product	-
Total	-	100	100

Endnotes

- ¹ The minimum percentage increases over time based on the type of facility and the year in which construction begins. For offshore wind projects, the requirement is 20% if the project begins construction prior to 2025; 27.5% if the project begins construction in 2025; 35% if the project begins construction in 2026; 45% if the project begins construction in 2027; and 55% if the project begins construction after 2027. For all other projects, the requirement is 40% if the project begins construction prior to 2025; 45% if the project begins construction in 2025; 50% if the project begins construction in 2026; and 55% if the project begins construction after 2026.
- ² Although "Production" is listed under the column for manufactured product components (MPCs), it is not a manufactured product component. "Production" refers to the production cost of the manufactured product and can only be included in the Adjusted Percentage Test if all of the manufactured product components of a manufactured product are domestically produced. See section 3.03(2) of Notice 2023-38.
- ³ Consistent with Notice 2023-38, the direct cost of producing a manufactured product counts toward the Adjusted Percentage Test only if all its manufactured product components are domestically produced.
- ⁴ For purposes of this table, module-level power electronics inverter systems, including either microinverters or direct current (DC) optimizers, are considered an inverter product.
- ⁵ Includes transformers, capacitors, inductors, bus/cables, circuit protection not on printed circuit board assemblies.
- ⁶ Flanges are typically made from single pieces of steel bar or pre-formed steel ingot; therefore the only component of a flange would be the steel material.