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IRS Issues Initial Guidance on Domestic Content Bonus Credit for Energy Projects

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The Inflation Reduction Act of 2022 (the “**IRA**”) added and modified certain renewable energy tax credit provisions of the U.S. Internal Revenue Code of 1986, as amended (the “**Code**”).¹ The IRA additions included a new domestic content bonus credit under Code Sections 45, 45Y, 48, and 48E (the “**Domestic Content Bonus Credit**”). Under these new rules, an increased credit amount or rate is available to (i) qualified facilities eligible for the Code Section 45 production tax credit (the “**PTC**”) and Code Section 45Y clean energy production credit (the “**CE PTC**”), (ii) energy projects eligible for the Code Section 48 investment tax credit (the “**ITC**”), and (iii) qualified investments with respect to qualified facilities or energy storage technology eligible for the Code Section 48E clean energy investment credit (the “**CE ITC**”) that satisfy the domestic content requirement set forth in Code Section 45 (incorporated by cross-reference in Code Section 48, which is incorporated by cross-reference in Code Section 48E) and in Code Section 45Y (the “**Domestic Content Requirement**”). In this Client Alert, we will refer to projects and facilities described in clauses (i)-(iii) of the previous sentence as “**Applicable Projects**.”

Under the IRA, a taxpayer will establish that the Domestic Content Requirement is satisfied with respect to an Applicable Project if it certifies to the Secretary of the Treasury that any steel, iron, or manufactured product that is a component of that Applicable Project (upon completion of construction) was produced in the United States (as determined under Section 661 of Title 49, Code of Federal Regulations²). As a result, the PTC or the CE PTC amount is increased by ten percent, and the energy percentage used to calculate the amount of the ITC or CE ITC is increased by two percentage points (or by ten percentage points if the Applicable Project either began construction before January 29, 2023 or satisfies certain wage and apprenticeship requirements).

On May 12, 2023, the Internal Revenue Service (the “**IRS**”) issued [IRS Notice 2023-38](#) (“**Notice 2023-38**”) to provide initial guidance on the Domestic Content Requirement.

Steel or Iron Requirement

Under Notice 2023-38, the Domestic Content Requirement with respect to steel or iron (the “**Steel or Iron Requirement**”) is met for an Applicable Project if all manufacturing processes with respect to any steel or iron items that are Applicable Project Components take place in the United States, except metallurgical processes involving refinement of steel additives. An “**Applicable Project Component**” is defined to mean any article, material, or supply, whether manufactured or unmanufactured, that is directly incorporated into an Applicable Project.

Notice 2023-38 also provides that the Steel or Iron Requirement applies to components that are construction materials made primarily of steel or iron and are structural in function, but not to steel or iron used in Manufactured Product Components (as defined below) or subcomponents of Manufactured Product Components. For example, items such as nuts, bolts, screws, washers, cabinets, covers, shelves, clamps, fittings, sleeves, adapters, tie wire, spacers, door hinges, and similar items that are made primarily of steel or iron but are not structural in function cannot be used to satisfy the Steel or Iron Requirement.

Table 2 of Notice 2023-38 (the “**Safe Harbor Classification Table**”) sets forth a nonexhaustive list of certain Applicable Project Components that may be found in utility-scale photovoltaic systems, land-based wind facilities, offshore wind facilities, and battery energy storage technologies. The Safe Harbor Classification Table categorizes the following Applicable Project Components as subject to the Steel or Iron Requirement:

Applicable Project Type	Applicable Project Components
Utility-scale photovoltaic system	<ul style="list-style-type: none"> • Steel photovoltaic module racking • Piles or ground screws • Steel or iron rebar in foundation (e.g., concrete pads)
Land-based wind facility	<ul style="list-style-type: none"> • Towers • Steel or iron rebar in foundation (e.g., spread footings)
Offshore wind facility	<ul style="list-style-type: none"> • Towers • Jacket foundation
Battery energy storage technology	<ul style="list-style-type: none"> • Steel or iron rebar in foundation (e.g., concrete pads)

Manufactured Products Requirement

A “**Manufactured Product**” for purposes of the Domestic Content Requirement is defined in Notice 2023-38 as an item produced as a result of the manufacturing process. Under Notice 2023-38, the Domestic Content Requirement with respect to Manufactured Products (the “**Manufactured Products Requirement**”) is met for an Applicable Project if all Applicable Project Components that are Manufactured Products are produced in the United States or are deemed produced in the United States.

For these purposes, a Manufactured Product is produced in the United States (a “**U.S. Manufactured Product**”) if (1) all of the manufacturing processes for the Manufactured Product take place in the United States and (2) all of the Manufactured Product Components of the Manufactured Product are of U.S. origin. A “**Manufactured Product Component**” is any article, material, or supply, whether manufactured or unmanufactured, that is directly incorporated into an Applicable Project Component that is a Manufactured Product. A component is considered to be of U.S. origin if it is manufactured in the United States, regardless of the origin of its subcomponents. Manufactured Products that are not U.S. Manufactured Products are “**Non-U.S. Manufactured Products.**”

I. Adjusted Percentage Rule

The IRA provides that Manufactured Products that are components of an Applicable Project upon completion of construction are deemed to have been produced in the United States if “not less than the adjusted percentage ... of the total costs of all such manufactured products of such facility are attributable to manufactured products (including components) which are mined, produced, or manufactured in the United States” (the “**Adjusted Percentage Rule**”). For the PTC and ITC, the adjusted percentage is 40% (20% in the case of an offshore wind facility). For the CE PTC and CE ITC,

the adjusted percentage increases from 40% (or 20%) to 55% based on an Applicable Project's beginning-of-construction date:

Beginning-of-Construction Date	Applicable Projects	Offshore Wind Facilities
Before 2025	40%	20%
In 2025	45%	27.5%
In 2026	50%	35%
In 2027	55%	45%
After 2027	55%	55%

Notice 2023-38 explains that the adjusted percentage for an Applicable Project is calculated as follows:

$$\frac{\text{Cost of U.S. Manufactured Products that are Applicable Project Components} + \text{Cost of U.S. Components}}{\text{Sum of cost of all Applicable Project Components that are Manufactured Products}}$$

A "**U.S. Component**" is a Manufactured Product Component of a Non-U.S. Manufactured Product that is an Applicable Project Component if the Manufactured Product Component is mined, produced, or manufactured in the United States.

For purposes of determining the cost of U.S. Manufactured Products and U.S. Components, a taxpayer may include only direct materials and direct labor costs that are paid or incurred (within the meaning of Code Section 461) by the U.S. Manufactured Product's manufacturer to produce the U.S. Manufactured Product or by the Non-U.S. Manufactured Product's manufacturer to produce or acquire the U.S. Component. A taxpayer may not include direct costs of incorporating the Applicable Project Components into the Applicable Project or direct costs incurred by the manufacturer to produce Non-U.S. Manufactured Products.

For purposes of determining the cost of all Applicable Project Components that are Manufactured Products, the cost of an Applicable Project Component includes only direct costs that are paid or incurred (within the meaning of Code Section 461) by the manufacturer of the Manufactured Product to produce the Manufactured Product.

The "manufacturer" for purposes of these rules is the person that performed the manufacturing process that produced the applicable Manufactured Product.

II. Safe Harbor Classifications

The Safe Harbor Classification Table categorizes the following Applicable Project Components as subject to the Manufactured Products Requirement:

Applicable Project Type	Applicable Project Components
Utility-scale photovoltaic system	<ul style="list-style-type: none"> • Photovoltaic trackers • Photovoltaic modules (which include the following Manufactured Product Components, if applicable: photovoltaic cells, mounting frame or backrail, glass, encapsulant, backsheet, junction box (including pigtailed and connectors), edge seals, pottants, adhesives, bus ribbons, and bypass diodes) • Inverters

Land-based wind facility	<ul style="list-style-type: none"> • Wind turbines (which include the following Manufactured Product Components, if applicable: the nacelle, blades, rotor hub, and power converter) • Wind tower flanges
Offshore wind facility	<ul style="list-style-type: none"> • Wind turbines (which include the following Manufactured Product Components, if applicable: the nacelle, blades, rotor hub, and power converter) • Wind tower flanges • Transition pieces • Monopiles • Inter-array cables • Offshore substations • Export cables
Battery energy storage technology	<ul style="list-style-type: none"> • Battery packs (which include the following Manufactured Product Components, if applicable: cells, packaging, thermal management system, and battery management system) • Battery containers/housing • Inverters

III. Retrofitted Projects

Under prior IRS guidance, an Applicable Project may qualify as originally placed in service even though it contains some used property, provided that the fair market value of the used property is not more than 20% of the Applicable Project’s total value, calculated by adding the cost of the new property to the value of the used property (the “**80/20 Rule**”). Sponsors and developers typically obtain a third-party appraisal to substantiate an Applicable Project’s qualification under the 80/20 Rule.

Notice 2023-38 provides that a retrofitted Applicable Project that is placed in service after 2022 and satisfies the 80/20 Rule is eligible for the Domestic Content Bonus Credit if the new property in the Applicable Project meets the Domestic Content Requirement and the taxpayer complies with the requirements described in Notice 2023-38.

Certification Procedures and Substantiation

Notice 2023-38 provides that to receive the Domestic Content Bonus Credit, a taxpayer must submit a statement to the IRS under penalty of perjury certifying that any steel or iron components subject to the Steel or Iron Requirement or Manufactured Products that are components of the Applicable Project upon completion of construction were produced in the United States. The certification statement must be attached to Form 8835, Form 3468, or other applicable form for reporting Domestic Content Bonus Credit amount filed with the taxpayer’s annual return submitted to the IRS for the first taxable year in which the taxpayer reports the Domestic Content Bonus Credit for an Applicable Project. For each subsequent taxable year in which a taxpayer claims the PTC or CE PTC with respect to the Applicable Project, the taxpayer must attach a copy of the certification statement. Notice 2023-38 also provides a list of information that must be included in the Domestic Content Bonus Credit certification statement, including the geographic coordinates and address of the Applicable Project and the date on which it was placed in service.

With respect to the timing of the certification, a taxpayer must certify that an Applicable Project satisfies the Domestic Content Requirement as of the date the Applicable Project is placed in service (i.e., the

date the Applicable Project is placed in a condition or state of readiness and availability for its specifically assigned function, whether in a trade or business or in the production of income).

It is not clear from Notice 2023-38 whether the transferor or transferee (or both) must complete and file the certification statement when a taxpayer transfers a credit to an unrelated party under Code Section 6418.

Notice 2023-38 also broadly provides that a taxpayer claiming the Domestic Content Bonus Credit amount must meet the general recordkeeping requirements of Code Section 6001 to substantiate that the Domestic Content Requirement has been met.

Future Guidance

The Department of the Treasury and the IRS intend to propose regulations addressing the rules applicable to the Domestic Content Bonus Credit, which the IRS expects will include the rules described in Notice 2023-38 as described above. These regulations are expected to apply to taxable years ending after May 12, 2023. In the meantime, taxpayers may rely on the rules described in Notice 2023-38 for any Applicable Project on which construction begins before the date that is 90 days after the publication of these proposed regulations (which, as noted, are expected to incorporate the rules described in Notice 2023-38).



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings Los Angeles lawyers:

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¹ For a general discussion on the additions and modifications introduced in the Inflation Reduction Act, see our prior Client Alert, [U.S. Senate Passes Inflation Reduction Act](#).

² Sections 661.1 through 661.21 of Title 49 of the Code of Federal Regulations, which are known as the Buy America Requirements, are administered by the Federal Transit Administration (FTA), Department of Transportation.

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