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IRS Expands Safe Harbor for Renewable Energy Projects

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In response to delays caused by COVID-19, the U.S. Internal Revenue Service (the “IRS”) has issued IRS Notice 2020-41 to extend both the “3-½ month” rule for the “beginning-of-construction” test and the continuity requirement for the production tax credit (“PTC”) and investment tax credit (“ITC”) for renewable energy facilities.

The U.S. Internal Revenue Code of 1986, as amended, provides for PTCs or, alternatively, ITCs, for renewable energy facilities. The amount of PTCs or ITCs a taxpayer may claim is based on when the facility begins construction. There are two tests—only one of which must be met—to determine when a project begins construction: (1) by making a significant beginning of physical work (the “Physical Work Test”), or (2) by paying or incurring at least 5% of the total cost of the energy property included in the facility (the “5% Safe Harbor Test”).

Both the Physical Work Test and the 5% Safe Harbor Test require that the taxpayer make continuous progress towards completion of the facility once construction has begun. In IRS Notice 2016-31, the IRS provided that if a taxpayer placed the facility in service within the calendar year that is no more than four calendar years after the calendar year during which construction of the facility began, the taxpayer would be considered to have made this continuous progress towards completion. In [IRS Notice 2020-41](#), the IRS has extended this period to five calendar years.

Under the 5% Safe Harbor Test, construction on a facility begins when the taxpayer pays or incurs (as those terms are used in Treasury Regulations section 1.461-1(a)(1) and (2)) at least 5% of the total cost of the energy property included in the facility (or services that may be included in the cost of such property). If the taxpayer pays the party from which it is receiving the energy property or services prior to receipt of that property or services, the taxpayer may treat the energy property or services as having been supplied (and thus construction of the facility having begun) if the taxpayer reasonably expects to receive that property or services within 3-½ months after the date of payment. A taxpayer’s reasonable expectation at the time of payment is relevant for purpose of this 3-½ month rule, and due to delays caused by COVID-19, [IRS Notice 2020-41](#) provides that if a taxpayer paid for energy property or services on or after September 16, 2019, the taxpayer will be deemed to have a reasonable expectation that that energy property or services would have been received within 3-½ months after the date of payment if the taxpayer receives the energy property by October 15, 2020.

Through IRS Notice 2020-41, the IRS has provided a greater level of comfort to taxpayers who develop and invest in renewable energy facilities that, despite delivery and construction delays caused



by COVID-19, renewable energy projects affected by the pandemic will satisfy the beginning-of-construction requirement.

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