

Client Alert

May 2020

IRS Notice 2020-41 Extends the Beginning of Construction Continuity Safe Harbor for Certain Renewable Energy Facilities

To address the unforeseen interruptions developers are now experiencing due to COVID-19, the Internal Revenue Service has issued [Notice 2020-41](#) (the “Notice”) extending and modifying the “beginning of construction” requirements for both the Section 45 production tax credit (“PTC”) and the Section 48 energy investment tax credit (“ITC”). For projects that started construction in either calendar year 2016 or 2017, the four-year continuity safe harbor described below is extended by one year.

Under current IRS guidance, taxpayers seeking to claim a PTC for electricity produced from qualifying facilities or an ITC for qualifying energy property, such as solar energy property, must generally begin construction of the qualifying facility or property by specified dates. A taxpayer is treated as having begun construction by starting physical work of a significant nature or, alternatively, by satisfying safe harbor requirements by incurring 5% or more of the total cost of the facility or property (the “5% safe harbor”). The taxpayer must then demonstrate continuous efforts or continuous physical work through the date that the facility is placed in service. IRS Notice 2017-04 provides a safe harbor under which the continuous efforts test or continuous physical work test is “deemed” to be satisfied if the facility is placed in service within four calendar years from the year in which construction begins (the “continuity safe harbor”).

The Notice extends and modifies the continuity safe harbor provided under existing guidance, for both the PTC and ITC, from four years to five years for projects that started construction in 2016 or 2017. For example, under the Notice if construction begins on a wind project in 2016, the taxpayer will have until December 31, 2021 to place the project in service and satisfy the continuity safe harbor. For a project that begins construction in 2017, the taxpayer will have until December 31, 2022 to place the property in service and satisfy the continuity safe harbor.

The Notice also extends the period of time that property or services can be delivered to a taxpayer under the economic performance rules of IRC § 461(h) for purposes of satisfying the 5% safe harbor. Taxpayers frequently rely on the “3½ Month Rule” under Treasury Regulation §1.461-4(d)(6)(ii) to treat costs as “incurred” for purposes of the 5% safe harbor in the year in which a cash payment for goods or services is made before the end of the year and the goods or services are reasonably expected to be delivered to the taxpayer within 3½ months of the payment. For example, a taxpayer may treat costs as incurred in 2019 for purposes of satisfying the 5% safe harbor in that year by making a cash payment before the end of the year as long as the taxpayer reasonably expects to take delivery of the goods or services within 3½ months of the payment. Many taxpayers seeking to begin construction of solar property in 2019 in order to qualify for the full 30% ITC made payments for solar equipment near the end of 2019 in reliance on the 3½ Month Rule. In many cases, the property was not delivered within the expected 3½ month period due to delays attributable to COVID-19.

The IRS emphasizes in the Notice that the 3½ Month Rule is satisfied if the taxpayer’s reasonable expectation at the time of the payment was that the person would provide the ordered services or property within 3½ months, regardless of any subsequent events that prevent that reasonable expectation from actually occurring. Nevertheless, to provide certainty and assurance, the Notice further provides

that for services or property paid for by the taxpayer on or after September 16, 2019, the taxpayer will be deemed to have had a reasonable expectation that the services or property would be received within 3½ months after the date of payment in the case of any services or property actually received by a taxpayer by October 15, 2020. The Notice provides that although this 3½ Month Safe Harbor will not apply to any services or property received by a taxpayer after October 15, 2020, the 3½ Month Rule may still be satisfied, as described above, based on reasonable expectations at the time of payment. The 3½ Month Safe Harbor applies only for purposes of the beginning of construction requirement for the PTC and the ITC.

If you have any questions about the Notice, prior guidance or Sections 45 or 48 generally, please contact us.

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