

December 29, 2023

Proposed Guidance on US Advanced Manufacturing Production Tax Credit

The US Inflation Reduction Act of 2022 (the “IRA”) established a credit Section 45X of the Internal Revenue Code for the US production and sale of eligible components of clean energy technologies, which include qualifying solar energy components (such as solar modules and photovoltaic cells), wind energy components (such as blades, nacelles, towers, offshore wind foundations and related offshore wind vessels), battery components (such as battery cells, battery modules and electrode active material) and applicable critical minerals (including lithium, nickel and aluminum)¹ (the “45X Credit”). The credit is available when eligible components are produced by a taxpayer and sold to an unrelated person, in each case as part of the taxpayer’s trade or business. The amount of the credit varies among eligible components, all of which, except for applicable critical minerals, are subject to a phase-out starting 2030 and sunset at the end of 2032. The 45X Credit is eligible to be sold to unrelated parties for cash and there is also a direct pay option under which qualifying taxpayers may receive a refund from the US government (for up to five years in the case of non-tax-exempt taxpayers).

On December 14, 2023, the Department of the Treasury and the Internal Revenue Service (“IRS”) released a Notice of Proposed Rulemaking regarding the 45X Credit, including much-needed guidance on what it means for an eligible component to be “produced by the taxpayer” and other requirements to be eligible for the credit. Interested parties may submit comments by February 13, 2024.

The guidance provides helpful certainty for solar, wind and battery component manufacturers and should also facilitate a market for the sale of the 45X Credits by these manufacturers to unrelated parties. However, the guidance does not fully address aspects of the 45X Credit for critical minerals and, as drafted, would not permit critical mineral producers to include raw material extraction costs within their production cost base when claiming the credit.

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A. Definitions

“Produced by the Taxpayer”

To be eligible for the 45X Credit, the eligible component must be “produced by the taxpayer.”² The proposed regulations provide that, in general, the term “produced by the taxpayer” requires the taxpayer to “substantially transform” (and not “partially transform”) constituent elements, materials or subcomponents into a complete and distinct eligible component that is functionally different from that which would result from mere assembly or superficial modification of the elements, materials or subcomponents.³ For solar grade polysilicon, electrode active materials and applicable critical minerals, the term “produced by the taxpayer” means processing, conversion, refinement or purification of source materials, such as brines, ores or waste streams, to derive a distinct eligible component.⁴

Generally, the taxpayer claiming the 45X Credit must be the person that performs the actual production activities that bring about a substantial transformation resulting in the eligible component and that sells such eligible component to an unrelated person.⁵ However, if the production is performed subject to a contract manufacturing agreement, then the parties may agree on which party will claim the 45X Credit.⁶

“Produced in the United States”

Another requirement for claiming the 45X Credit is that the eligible components be produced within the United States or a possession of the United States.⁷ The proposed regulations clarify that constituent elements, materials and subcomponents used in the production of eligible components are not subject to this requirement. In other words, manufacturers would be able to import constituent elements, materials or subcomponents (such as lithium hydroxide) used in the production process and claim the 45X Credit for the resulting eligible component (such as a battery component that uses the imported lithium hydroxide). However, they would not be able to claim the 45X Credit for the costs of the imported constituent elements, materials or subcomponents since they were not “produced in the United States.” Moreover, elements, materials and subcomponents used in the production of eligible components can be from recycled sources rather than newly created.⁸ Ultimately, the 45X Credit would allow for more flexibility compared to the clean vehicle credit under 26 U.S. Code § 30D, which has various limitations on non-US content in the supply chain.

“Integrated, Incorporated, or Assembled”

The proposed regulations provide that a taxpayer is treated as having produced and sold an eligible component to an unrelated person (and thus is eligible for the 45X Credit) if such component is “integrated, incorporated, or assembled” into another eligible component that is then sold to an unrelated person. The term “integrated, incorporated, or assembled” is further defined to mean the production activities by which eligible components that are constituent elements, materials or subcomponents are substantially transformed into another complete and distinct eligible component functionally different from that which would result from mere assembly or superficial modification of the eligible components and other elements, materials or subcomponents.⁹

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B. Sale to an Unrelated Person

In order to claim the 45X Credit, the eligible component must be sold by the taxpayer to an unrelated person.¹⁰ However, the taxpayer may make an election to treat a sale to a related person (for example, between members of the same consolidated group) as a sale to an unrelated person solely for purposes of the 45X Credit (the “Related Person Election”).¹¹ The Related Person Election must generally be made annually in Form 7207, *Advanced Manufacturing Production Credit*, and filed with the taxpayer’s timely filed original tax return (including extensions).¹² Moreover, there is an anti-abuse rule that would make the Related Person Election unavailable in extraordinary cases where a taxpayer seeks to exploit the 45X Credit in an “improper and wasteful manner” (i.e., a use that is wasteful, such as disregarding, disposing of or destroying the eligible component without putting it to a productive use) or sell defective components (i.e., components that do not meet the requirements of §45X) to a related person.¹³ The taxpayer must provide all required information set forth in the guidance, such as information regarding the taxpayer and the related person, eligible components being sold and the intended purpose of the sales.¹⁴

C. Credit Amount

Certain 45X Credit amounts are equal to “10 percent of the costs” of production of the specific eligible component (such as electrode active materials and critical minerals). The proposed regulations clarify that the production costs would not include any costs incurred after such production (such as the costs to incorporate the electrode active material into a battery component or to incorporate the applicable critical mineral into another product).¹⁵ Moreover, direct or indirect material costs, and any costs related to the extraction or acquisition of raw materials, would also not be taken into account as production costs. The Department of the Treasury and the IRS request further comments on how the costs of extraction and other similar value-added activities should be includible that would protect against duplication of credit amounts across the production chain.

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ENDNOTES

- 1 Applicable critical minerals include specified forms of aluminum, antimony, arsenic, barite, beryllium, bismuth, cerium, cesium, chromium, cobalt, dysprosium, erbium, europium, fluorspar, gadolinium, gallium, germanium, graphite, hafnium, holmium, indium, iridium, lanthanum, lithium, lutetium, magnesium, manganese, neodymium, nickel, niobium, palladium, platinum, praseodymium, rhodium, rubidium, ruthenium, samarium, scandium, tantalum, tellurium, terbium, thulium, tin, titanium, tungsten, vanadium, ytterbium, yttrium, zinc and zirconium.
- 2 IRC §45X(a)(1)(A).
- 3 Prop. Reg. §1.45X-1(c)(1).
- 4 Prop. Reg. §1.45X-1(c)(2).
- 5 Prop. Reg. §1.45X-1(c)(3)(i).
- 6 Prop. Reg. §1.45X-1(c)(3)(ii)(A), (c)(3)(iii). A “contract manufacturing arrangement” is any agreement providing for the production of an eligible component if the agreement is entered into before the production of the eligible component to be delivered under the contract is completed. Prop. Reg. §1.45X-1(c)(3)(ii)(B).
- 7 IRC §45X(d)(2).
- 8 Prop. Reg. §1.45X-1(d)(2).
- 9 Prop. Reg. §1.45X-1(f)(1).
- 10 IRC §45X(a)(1)(B); Prop. Reg. §1.45X-2(a).
- 11 IRC §45X(a)(3)(B)(i). Also, if the taxpayer sells an eligible component to a related person who later sells the component to an unrelated person, then the sale to the taxpayer’s related person will be treated as a sale to an unrelated person. IRC §45X(a)(3)(A).
- 12 Prop. Reg. §1.45X-2(d)(2).
- 13 Prop. Reg. §1.45X-2(d)(4).
- 14 Prop. Reg. §1.45X-2(d)(2)(ii).
- 15 Prop. Reg. §§1.45X-3(e)(2)(ii)–(iv); 1.45X-4(c)(3).

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