

Sales And Use Tax Strategies For Renewables After OBBBA

By Karey Barton, Sarah Vergel de Dios and Sarah Horn (September 18, 2025, 4:23 PM EDT)

For decades, federal tax incentives have been a key driver of solar and wind energy project development. The Inflation Reduction Act, passed in 2022, marked one of the most significant expansions of those incentives, with developers expecting Section 45Y production tax credits and Section 48E investment tax credits to run well into the next decade, and be readily monetized.[1]

The recently enacted One Big Beautiful Bill Act sharply curtails these incentives, heightening the importance of managing sales and use tax risks and opportunities.[2] The OBBBA shortens the timeline for federal support, and adds new hurdles for solar and wind projects.[3]

Under the OBBBA, a solar or wind project qualifies for these credits only if it: (1) starts construction by July 4, 2026, or is placed in service before 2028; and (2) avoids significant equipment or ownership links to prohibited foreign entities.[4]

The OBBBA also phases in a higher Section 48E domestic content adder threshold, making it more difficult for projects to qualify for the additional credit amounts.

Consistent with Executive Order No. 14315, the IRS issued Notice 2025-42 on Aug. 15, eliminating the long-standing 5% cost safe harbor for establishing beginning of construction for most projects, and further compressing taxpayer timelines. Projects therefore must show earlier, verifiable physical work and maintain progress to retain credit eligibility.[5]

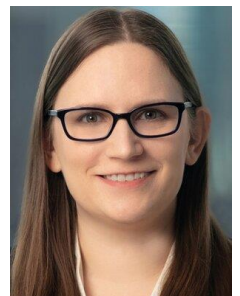
Together, these provisions create a compressed, front-loaded development window. Developers are scrambling to lock up supply chains; execute engineering, procurement and construction contracts; and document construction activity early to preserve credit eligibility before stricter eligibility requirements apply and the credits expire altogether.

At the same time, higher U.S. tariffs on imported components are inflating equipment costs and, in certain jurisdictions and certain circumstances, may increase the sales and use tax base.

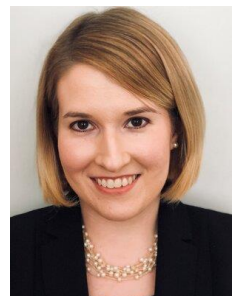
And with federal benefits shrinking and compliance burdens rising, an unexpected 6% to 10% sales or use tax hit on costly materials and certain services can erode what remains of project margin. Managing



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these transaction tax exposures is central to project economics in the post-OBBA environment.

Common Sales and Use Tax Pitfalls in Renewable Energy Project Development

Forty-five states and the District of Columbia currently impose state-level sales and use taxes, and many local governments also levy additional taxes, resulting in combined rates that exceed 10% in some areas.[6]

These taxes reach beyond tangible personal property, or TPP, to specifically enumerated services, which often include repair and maintenance, and may also extend to freight, installation and other incidental charges.

Because tax is imposed at the legal entity level, transfers of taxable items or services between affiliates are generally treated as taxable events unless a statutory exemption applies. Early modeling and careful structuring are essential to avoid costly surprises; missteps may surface later as unexpected assessments, penalties and interest.

Three exemption regimes drive most planning for solar and wind energy projects: manufacturing exemptions, renewables-specific exemptions, and resale exemptions or exclusions.

Manufacturing exemptions, available in most states, often require both that the purchaser be engaged in manufacturing and that the equipment be used in producing TPP for sale. The exemption extends to power generators in many states, as electricity often meets the definition of TPP.

However, notable outliers — such as Illinois, Connecticut and Colorado — do not treat power generation as an exempt manufacturing activity.[7] California takes a different tack, offering only a capped, partial manufacturing exemption calculated on a combined-entity basis, and the state is aggressively enforcing the cap.[8]

Not all solar or wind projects qualify for these manufacturing exemptions. The project type and power offtake structure can affect eligibility.

A handful of states, including New York, Connecticut and Colorado, layer on renewables-specific exemptions aimed at promoting clean energy development. Yet these incentives are often technology- or component-specific. For example, a solar array may qualify where a wind facility does not, or vice versa.[9]

Published guidance does not always clearly define what qualifies for manufacturing or renewables exemptions, leaving project owners to navigate ambiguity when applying these exemptions. This can be especially significant for high-value items like batteries or trackers, which may qualify in some states but not others.

Finally, meeting state requirements for resale exemptions is essential for tax-free intercompany transfers. A single break in that chain can convert the transfer into a taxable event.

The crucial analysis lies in understanding and maximizing the available exemptions, and planning for the sales and use tax impacts when modeling, negotiating contracts and assessing overall project economics.

Successfully managing transaction tax on these projects requires a close look at several key issues that arise during project development and operation.

Classification of the Project: TPP vs. Real Property

A project's sales and use tax posture turns first on whether its equipment is treated as TPP or real property, which depends on both the characteristics of the project and state-specific standards.

Texas applies a three-part test — annexation, adaptation and intent — to determine whether equipment becomes real property upon installation. A utility-scale solar farm may qualify as real property, while easily removable rooftop panels may remain TPP.

While the considerations are often similar, states apply different standards to determine property classification. Ohio generally considers any property that primarily benefits the business conducted on the land, rather than the land itself, to remain TPP, even when permanently affixed to real property.[10]

California splits installations into materials, which become real property, and fixtures, which stay identifiable, taxing each differently.[11]

Classification drives every downstream tax issue. During construction, the classification determines how both labor and materials are taxed.

Texas does not tax labor for new construction of real property, but installation performed by a seller of TPP becomes taxable as part of the sales price of any nonexempt equipment.[12] In many states, classification also affects the party responsible for paying tax and claiming exemptions.[13]

Classification likewise governs the taxability of maintenance and repairs. In Texas, otherwise taxable repairs and maintenance to renewable energy TPP may qualify for exemption if the TPP itself is exempt.[14]

In contrast, real property repair labor is generally taxable regardless of the exemption status of the repaired property, although narrow exclusions exist for certain scheduled and periodic preventive maintenance.[15]

The classification may also affect sale-leaseback transactions commonly used in tax equity financing. Leases of real property are typically not taxed, but leases of TPP may be taxable unless the transaction meets certain state-specific requirements for treatment as a nontaxable financing arrangement.[16]

Additional complications may arise if the sale-leaseback deal occurs after the project becomes operational, as a project owner may not be eligible to claim a resale exemption on equipment it used prior to a sale-leaseback transaction.

Early review of the project classification sets the stage for informed tax decisions.

Procurement Structure

Because exemption availability varies across the supply chain, optimizing procurement structure is essential. Purchasing equipment through the wrong entity can jeopardize exemptions.

Texas, for example, limits the manufacturing exemption to legal entities that are engaged in manufacturing. California offers a capped, partial exemption for qualified manufacturers that is calculated on a combined-entity basis, and the state is actively enforcing the cap.

Exemption benefits also hinge on how equipment moves through the corporate structure. Each transfer between legal entities must be properly executed and documented to meet state rules.

If a link in that chain involves an entity that lacks the ability to claim an exemption or there is no true sale as defined under state law, the handoff can trigger unexpected taxes.

Even temporary storage may be a taxable use in some states unless an exemption applies. Where temporary storage exemptions are unavailable, meeting the requirements for resale, manufacturing or renewables exemptions is necessary to minimize tax during storage.

Aligning purchasing entities, carefully planning intercompany transfers and arranging storage to comply with each state's rules is critical to preserving exemptions and minimizing tax exposure.

Construction Contracts and Installation

States have unique rules for materials and equipment procured through a construction contract for real property, often focused on whether the contractor is deemed to be a consumer or retailer of those items. This determination can vary based on contract type and terms, and some states do not allow exemptions to flow through to the contractor.

Texas distinguishes between lump-sum and separated contracts for new construction. Under a lump-sum contract, the contractor is the consumer of materials and equipment incorporated into real property, and cannot claim the manufacturing exemption.

Only with a separated contract, which requires specific provisions in the contract, can the manufacturing exemption be preserved, making early and precise contract planning essential.[17] Sufficient pricing detail, whether in invoices, priced equipment lists or the contract itself, is also necessary to claim any exemptions.

Different rules apply to the sale and installation of equipment that remains TPP. In many states, including Texas, installation performed by a seller of TPP becomes part of the tax base of the TPP.[18]

By contrast, California generally excludes installation labor from tax but imposes tax on fabrication labor to create, produce, process or assemble TPP.[19]

Because these state-by-state differences govern whether exemptions survive, developers must tailor engineering, procurement and construction contracts, change orders and supporting documentation to each jurisdiction, and clearly document taxable versus nontaxable charges to maximize exemptions.

Operations

Once the project is operational, new issues arise that can create ongoing indirect tax requirements or exposures.

Operations and maintenance contracts often include a mix of services, such as operations, repairs,

preventative maintenance and vegetation management, along with replacement parts, spares or other TPP, typically for a single periodic charge.

The taxability of these charges varies by state and by the classification of the property. For example, in Texas, scheduled and periodic maintenance services for real property are nontaxable, while in New Mexico, service providers must pay gross receipts tax on these charges and typically pass the cost on to the purchaser.[20]

The taxability of operations and maintenance services performed on TPP may require consideration of the initial taxability of the underlying equipment. If the transaction is bundled and lacks sufficient supporting documentation, the entire charge may be taxable, even if some components would otherwise be nontaxable or exempt.

Additionally, varying state rules for contractors and repair providers affect the treatment of materials. Many states also have special rules for warranty repairs, which can further complicate the analysis for operations and maintenance contracts.

The sale of electricity under a power purchase agreement can also trigger sales, use or gross receipts tax obligations, depending on the state and transaction structure.

In many states, electricity is classified as TPP, and direct sales to end users under a power purchase agreement may require the project entity to register and collect sales tax unless an exemption applies.[21] For exempt sales, maintaining appropriate documentation is essential.

While these smaller periodic charges may be overlooked from a sales tax perspective, the impact can be significant over time. Appropriately structuring contracts and supporting documentation can provide substantial savings throughout the project's operational phase.

Leading Practice Playbook

In the post-OBBA world, the following leading practices can help create a solid framework for managing sales and use tax exposure in renewables projects.

Plan proactively and conduct a tax analysis early.

Engaging in a detailed analysis of tax implications at the outset helps identify available exemptions, mitigate double taxation, and anticipate audit or tax equity scrutiny.

Special attention is warranted in California, where the partial exemption is narrowing, and in states that permit rate-reduction tools such as Texas, with its direct pay permits, or Colorado, with its point-of-delivery structures.

Certain states may also provide application-based credit and incentive programs that must be in place early in project development.

Preserve exemptions through contract and procurement structure and documentation.

Careful engineering, procurement and construction contract drafting, particularly in Texas, and a clearly mapped procurement flow are essential to maintain statutory exemptions and withstand audit review.

Document exemptions and obtain certificates contemporaneously to avoid penalties.

Monitor legislative updates.

Ongoing tracking of federal and state legislative and administrative updates is critical, as mid-project shifts can alter the tax base or available exemptions.

Revisit taxability when operations begin.

The start of power sales, operations and maintenance services, and warranty replacements can create new indirect tax obligations that should be evaluated soon after commercial operations begin.

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[1] Pub. L. No. 117-169.

[2] Pub. L. No. 119-21.

[3] Credit phaseouts for battery and energy storage projects remain unchanged by the new provisions.

[4] Pub. L. No. 119-21.

[5] IRS Notice 2025-42.

[6] Tax Foundation, 2025 Sales Tax Rates, Sales Taxes by State.

[7] Ill. Admin. Code tit. 86, §130.330(k); Dep't of Revenue v. Pub. Serv. Co. of Colorado, 330 P.3d 385 (Colo. 2014); United Illuminating Co. v. Groppo, 220 Conn. 749, 601 A.2d 1005 (1992); Connecticut Department of Revenue Services Ruling 2004-2 (June 18, 2004).

[8] Cal. Rev. & Tax. Cd. § 6377.1; Cal. Code Regs. 1525.4.

[9] C.R.S. 39-26-724; Conn. Gen. Stat. §12-412(117); N.Y. Tax Law § 1115(ii)(1).

[10] Ohio Admin. Code 5703-9-14(B).

[11] Cal. Code Regs. tit. 18, § 1521(a)(4)-(5).

[12] Tex. Tax Code 151.007(a)(3); 34 Tex. Admin. Code 3.291(b).

[13] Massachusetts Department of Revenue, Letter Ruling 06-3 (April 7, 2006).

[14] 34 Tex. Admin. Code 3.292(b).

[15] 34 Tex. Admin. Code 3.357(b)-(c).

[16] Cal. Code Regs. 1660; Texas Comptroller of Public Accounts, Letter No. 9609L1430D03 (Sept. 24, 1996).

[17] 34 Tex. Admin. Code § 3.291(b)(3)-(4).

[18] Tex. Tax Code Ann. § 151.007(a)(2).

[19] Cal. Code Regs. tit. 18, § 1546(a).

[20] 34 Tex. Admin. Code 3.357(b)-(c); N.M. Admin. Code 3.2.1.18(A).

[21] See, e.g., Tex. Tax Code § 151.009.