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Court Vacates IRS Beginning-of-Construction Rules, but Renewable Energy Developers Should Be Cautious

A federal court has vacated IRS Notice 2025-42, which had eliminated one of two safe harbors that wind and solar energy developers could use to establish beginning-of-construction for their projects. Under the Notice, the 5% of project costs safe harbor was eliminated, leaving only the physical work test available. With a looming deadline to begin construction by July 4, 2026 (or else be placed in service by December 31, 2027) to qualify for the I.R.C. § 45Y production tax credit or § 48E investment tax credit, the potential reinstatement of the 5% safe harbor is a welcome development. Nevertheless, developers should be wary of relying on this ruling.

On June 6, in *Oregon Environmental Council v. IRS*, the United States District Court for the District of Columbia vacated the Notice. The court found that the Notice was arbitrary and capricious because it eliminated the safe harbor for wind and solar projects without developing an administrative record accounting for the industry's reliance interest on prior notice or adequately explaining the reasons for the safe harbor's removal. The court further held that the Notice's assertion that some industry participants were "circumventing" statutory cutoffs or engaging in "artificial manipulation of eligibility" was not supported by the record.

This ruling does not mean that the 5% safe harbor will necessarily be available, however. First, the appeal deadline for this order has not yet passed and will not pass until after the July 4 deadline. Second, even if the government does not appeal, or does not succeed on appeal, the IRS has authority in some circumstances to issue orders that are effective retroactively. It is not out of the

question that IRS will correct the identified defects and issue a new notice purporting to eliminate the 5% safe harbor as of the original effective date.

What this means to you

It would be risky for industry participants to rely on this order and assume the 5% safe harbor is available. The better practice is to continue relying on any physical work strategy already in place. But for projects that would otherwise be unable to meet the physical work test, or where there are questions about whether their physical work was adequate, developers may want to consider whether the 5% safe harbor offers them a new avenue to meeting the beginning-of-construction test.

Contact us

For further details or additional information, contact Andrew Eastman, Doug Jones, Jason Reschly, Robert Romashko, or another member of the Husch Blackwell tax team.