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Treasury Guidance Tightens "Beginning of Construction" Standards for Clean Energy Tax Credits, Eliminating 5% Safe Harbor for Wind and Solar Projects

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On August 15, 2025, the Internal Revenue Service (IRS) issued Notice 2025-42, providing long-awaited guidance on the “beginning of construction” requirements for wind and solar facilities under Sections 45Y and 48E of the Internal Revenue Code, as amended by the One Big Beautiful Bill Act (OBBBA). The notice, effective for projects that do not begin construction under prior IRS guidance before September 2, 2025, largely preserves the existing physical work test but significantly limits the use of the five percent safe harbor to small solar projects with a nameplate capacity of 1.5 MW or less.

Background

The notice was issued in response to Executive Order 14315 (“Ending Market Distorting Subsidies for Unreliable, Foreign-Controlled Energy Sources”), issued on July 7, 2025. As we discussed previously, the executive order directed the Secretary of the Treasury to “strictly enforce” the termination of Section 45Y production tax credits and Section 48E investment tax credits for wind and solar facilities and to issue updated guidance within 45 days specifically aimed at clarifying and tightening the “beginning of construction” rules for energy projects. Additionally, the Treasury Secretary was required to promptly implement more stringent restrictions on foreign entities of concern (FEOC), as mandated by the OBBBA.

As amended by the notice, the IRS previously issued a series of notices (e.g., Notice 2013-29 and Notice 2018-59) that provided guidance for determining when a project is deemed to have begun construction. According to these notices, two methods are available for establishing the commencement of construction: the Physical Work Test and the Five Percent Safe Harbor. The Physical Work Test is met—and construction is considered to have started—when physical work of a significant nature commences on property that forms an integral part of the activity to be performed at the energy facility. In contrast, under the Five Percent Safe Harbor, construction is deemed to have begun when the taxpayer incurs five percent or more of the total cost of the energy property.

Key provisions of notice 2025-42

The notice modifies prior IRS guidance concerning the “beginning of construction” criteria as it relates to the credit termination provisions introduced by the OBBBA under Sections 45Y and 48E of the Internal Revenue Code.

The Five Percent Safe Harbor

Effective September 2, 2025, only solar projects with a nameplate capacity of 1.5 MW (AC) or less may use the five percent safe harbor. Large wind and solar projects must instead satisfy the Physical Work Test. Developers of larger projects seeking to rely on the five percent safe harbor must begin construction under prior guidance before September 2, 2025.

The Physical Work Test

The Physical Work Test remains largely unchanged from previous IRS guidance. Physical work of a significant nature may be conducted either on-site or off-site. For wind projects, activities satisfying the requirements include excavation of turbine foundations, installation of anchor bolts, or pouring of concrete pads; for solar projects, activities include the assembly of racks or other supporting structures to secure photovoltaic panels, collectors, or solar cells. For a detailed analysis of the Physical Work Test’s application within the OBBBA framework, please refer to our blog [here](#).

Continuity requirement

Like the Physical Work Test, the continuity requirement is left mostly unchanged. The continuity requirement requires that projects be placed in service by the end of the calendar year that is four years after the year in which the project began construction.

FEOC rules

The notice does not address the application of the beginning of construction standard for purposes of the new FEOC framework under the OBBA. In a footnote, the notice explains that future guidance will come regarding the beginning of construction requirement under the FEOC Equipment Rule. Until

such guidance is issued, it appears that taxpayers may generally rely on the notice for establishing the beginning of construction for FEOC purposes.

Contact us

If you have any questions about the new beginning of construction standards or other clean energy tax issues, contact Doug Jones, Jakob Seidler, or your local Husch Blackwell attorney.