

IRS Publishes Guidance for Determining Beginning of Construction for Solar and Wind Projects

On August 15, 2025, the Internal Revenue Service (“IRS”) issued Notice 2025-42 (the “New Guidance”) providing guidance on the “beginning of construction” requirements for solar and wind projects to qualify for clean electricity production credits under Section 45Y (“Clean Electricity Production Credits”), and clean electricity investment credits under Section 48E (“Clean Electricity Investment Credits”, together with Clean Electricity Production Credits, the “Production and Investment Credits”), of the Internal Revenue Code (the “Code”). The New Guidance is more restrictive than previous guidance issued under past IRS notices (together, the “Legacy Guidance”),¹ as it does not permit the use of the Five Percent Safe Harbor (as defined below) to establish beginning of construction. However, the New Guidance only applies to wind and solar facilities that begin construction on or after September 2, 2025 and does not apply retroactively to projects that established beginning of construction prior to September 2, 2025 based on the Five Percent Safe Harbor.

EXECUTIVE SUMMARY

- The New Guidance applies only to wind or solar projects that begin construction on or after September 2, 2025 and does not apply to other clean energy technologies that are eligible to claim Production and Investment Credits, which will continue to apply the Legacy Guidance.
- For solar and wind facilities that begin construction between September 2, 2025 and July 4, 2026, the Physical Work Test (as defined below) is the sole method available to establish that construction was commenced during such period.
- Smaller solar projects (projects with a maximum net output no greater than 1.5 MW AC) that begin construction between September 2, 2025 and July 4, 2026 can establish the beginning of construction by satisfying either the Physical Work Test or the Five Percent Safe Harbor (as defined below).
- For solar and wind projects that began construction prior to September 2, 2025, both the Physical Work Test and Five Percent Safe Harbor remain valid methods to establish the beginning of construction, and the New Guidance does not retroactively alter those determinations.

- Taxpayers must meet the Continuity Requirement (as defined below) to be eligible for the wind and solar Production and Investment Credits, but the Continuity Requirement may be deemed to have been met if the project is placed in service within four years after the beginning of construction.
- The Department of the Treasury (“Treasury”) is in the process of drafting separate guidance related to the new FEOC restrictions under the OBBBA (both as defined below).

BACKGROUND

The One Big Beautiful Bill Act (“OBBBA”) was signed into law on July 4, 2025, significantly curtailing the availability of federal clean energy tax credits and introducing new restrictions on foreign entities of concern (“FEOC”) (see our previous memo on the OBBBA [here](#)). Under the OBBBA, Production and Investment Credits for wind and solar facilities are only available for projects that begin construction by July 4, 2026 (*i.e.*, 12 months after the enactment of the OBBBA) or that are placed in service by December 31, 2027.

On July 7, 2025, President Trump issued Executive Order 14315, *Ending Market Distorting Subsidies for Unreliable, Foreign-Controlled Energy Sources* (the “Order”), directing Treasury to take all action necessary and appropriate within 45 days of enactment of the OBBBA to strictly enforce termination of the Production and Investment Credits for solar and wind facilities, including the issuance of new and revised guidance to curtail abuse of the beginning of construction rules.

Prior to the enactment of the OBBBA, a taxpayer could establish the beginning of construction for solar or wind projects if either the “Physical Work Test” or the “Five Percent Safe Harbor” were satisfied. In addition, the taxpayer was required to meet a continuity requirement by demonstrating ongoing progress toward a project’s completion after beginning construction (the “Continuity

Requirement”). Taxpayers were deemed to have met the Continuity Requirement if the project was placed in service by the end of the fourth calendar year after the calendar year in which construction began (the “Continuity Safe Harbor”).

NEW GUIDANCE

The New Guidance is applicable for solar and wind projects that commence construction after September 2, 2025. With an exception for low-output solar, the New Guidance establishes the Physical Work Test as the exclusive method for establishing that construction on a solar or wind facility began prior to July 5, 2026 (and therefore such facility is not subject to the December 31, 2027 placed-in-service deadline). For solar facilities with a maximum net output of 1.5 megawatts or less taxpayers may satisfy either the Physical Work Test or the Five Percent Safe Harbor to establish the beginning of construction.

The “Physical Work Test” is a facts-and-circumstances test that requires taxpayers to have performed physical work of a “significant nature” on the project. The Physical Work Test takes into consideration the nature of the work performed. There is no quantitative threshold for work performed or money invested to satisfy the test. The New Guidance maintains strict requirements for on-site and off-site work to qualify as work of a “significant nature” and provides examples of physical work that would qualify.

- For wind projects, qualifying physical work includes on-site foundation excavation, anchor bolt installation and concrete pad pouring. Qualifying off-site physical work includes the manufacture of wind turbine components specifically for the project or the manufacture of transformers or power conditioning equipment.
- For solar projects, qualifying physical work includes on-site foundation excavation or installation of racks, rails, supports or solar cells. Qualifying off-site physical work includes the manufacture of mounting equipment, inverters and transformers.

- Preliminary activities such as planning, permitting, financing, site clearing, geotechnical testing or work on inventory components are excluded as qualifying physical work.
- Work for manufacturing, construction or production of property by a third party under a binding written contract will be taken into account in determining whether physical work of a significant nature has taken place, provided that such contract does not limit damages to a specified amount. A contract will not be treated as limiting damages to a specified amount if damages are limited to at least five percent of the total contract price.

Under the “Five Percent Safe Harbor,” taxpayers are deemed to have begun construction when they have paid or incurred five percent or more of the total project cost.

Under both the Physical Work Test and Five Percent Safe Harbor, the taxpayer is required to also meet the Continuity Requirement in order to be eligible for the Production and Investment Credits. This can be satisfied by either meeting the four-year, placed-in-service deadline to qualify for the Continuity Safe Harbor or otherwise maintaining a continuous program of construction. The New Guidance eliminates the ability of taxpayers to satisfy the Continuity Requirement by demonstrating “continuous efforts” (*i.e.*, through activities such as permitting, securing financing and negotiating contract), as was available under Legacy Guidance, and instead requires the taxpayer to demonstrate ongoing physical work of a significant nature until completion of the project.

The New Guidance recognizes excusable delays outside a taxpayer’s control that will not be considered for the purpose of satisfying the Continuity Requirement—*e.g.*, natural disasters, financing delays, interconnection delays, supply chain shortages or permitting issues. However, such excusable delay does not extend the four-year window for a project to be placed in service under the Continuity Safe Harbor.

Solar or wind facilities that begin construction after July 4, 2026 must be placed in service by no later than December 13, 2027 in order to qualify for the Production and Investment Credits. For solar or

wind facilities that began construction prior to September 2, 2025, the more restrictive beginning of construction requirements under the New Guidance will not apply and the Legacy Guidance will continue to apply. This approach alleviates industry concerns that the IRS would apply the new rules retroactively to projects that established beginning of construction based on the Five Percent Safe Harbor prior to the enactment of the OBBBA or issuance of the Order.

The New Guidance does not affect the beginning-of-construction rules for assets other than solar or wind, and other clean energy technologies that are eligible to claim Production and Investment Credits will continue to apply the Legacy Guidance to establish the beginning of construction. The New Guidance also does not apply to other aspects of the OBBBA, such as FEOC restrictions. A footnote included in the New Guidance explains that separate guidance on the beginning-of-construction rules applicable to FEOC restrictions is in the process of being drafted by Treasury.

CONCLUSION

The New Guidance limits the strategies and options available to solar and wind developers to establish the beginning-of-construction date and preserve eligibility for the solar and wind Production and Investment Credits. While the IRS has set out specific examples of qualifying physical work, the “significant nature” standard remains fact-specific and will likely be tested under the Order’s directive of strict scrutiny.

The elimination of the Five Percent Safe Harbor for all but small solar projects may heighten capital and permitting requirements for projects to demonstrate the beginning of construction; however, experienced developers and investors are familiar with the qualification requirements of the Physical Work Test and will be able to rely on strategies that have been developed over the past decade. Developers and investors should expect continued industry emphasis on accelerating project development and should take proactive steps to manage permitting, financing and documentation to preserve credit eligibility in an increasingly complex regulatory environment.

1 See Notice 2022-61, which incorporates prior IRS notices providing guidance on establishing the beginning of construction date.

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