



Tax Insights
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Services

Invalidated IRS Notice 2025-42 creates uncertainty for wind and solar credit projects

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In brief

What happened?

The US District Court for the District of Columbia on June 6 issued a decision in *Oregon Environmental Council v. IRS*, vacating Notice 2025-42 in its entirety and remanding the matter to Treasury and the IRS for further consideration. The court held that Notice 2025-42, which had eliminated the Five Percent Safe Harbor as a method for establishing the beginning of construction (BOC) for most wind and solar projects under Sections 45Y and 48E, was arbitrary and capricious in violation of the Administrative Procedure Act (APA).

Why is it relevant?

As amended by the “One Big Beautiful Bill Act” (OBBBA), wind and solar facilities eligible for Section 45Y and 48E clean electricity credits generally must be placed in service before January 1, 2028, unless construction of the facilities begins before July 5, 2026. The court's decision restores, at least for now, the long-standing dual-method framework under Notice 2013-29 and its successors that allows taxpayers to establish BOC for wind and solar projects using either the Physical Work Test or the Five Percent Safe

Harbor. Invalidation of Notice 2025-42 benefits developers, investors, and other stakeholders that otherwise would have been required to redesign or accelerate projects to meet the Physical Work Test.

Observation: Given the timing of the court's decision, the practical benefit of the restored Five Percent Safe Harbor may be limited for taxpayers that have not already incurred sufficient eligible costs before the BOC deadline of July 5, 2026.

Actions to consider

Taxpayers should consider the impact of the court's decision and assess the ability of current and planned wind and solar projects to satisfy the Five Percent Safe Harbor. Because the decision still could be appealed, however, a prudent course for most developers may be to preserve flexibility under both methods rather than switching methods based on the court's ruling, which could be stayed, modified, or reversed. Continued engagement with contractors, suppliers, and tax equity investors will be important as legal clarity develops.

In detail

Background

As originally enacted, the full value of the Section 45Y Clean Electricity Production Credit and the Section 48E Clean Electricity Investment Credits generally was available to qualifying zero-emission electricity generating facilities for which construction began before the end of 2033, regardless of underlying technology (e.g., solar, wind, nuclear, hydropower).

The OBBBA, signed into law on July 4, 2025, accelerated the sunset date of Sections 45Y and 48E credits by terminating the credits for wind and solar facilities placed in service after December 31, 2027. However, if construction begins before July 5, 2026, then wind and solar facilities generally may use a four-year Continuity Safe Harbor or the facts and circumstances test to satisfy the BOC requirements. An executive order issued on July 7, 2025 (Executive Order), directed Treasury to strictly enforce these new termination provisions and to issue guidance preventing manipulation or artificial acceleration of project eligibility.

BOC framework

Since 2013, the IRS has consistently recognized two methods by which a taxpayer may establish BOC:

- The Physical Work Test: Established by starting "physical work of a significant nature"
- The Five Percent Safe Harbor: Established by paying or incurring 5% or more of the total cost of the facility before the statutory deadline.

Both methods also require the taxpayer to satisfy the Continuity Requirement. The Continuity Requirement may be satisfied either by placing a facility in service within four years after beginning

construction (Continuity Safe Harbor) or under a facts and circumstances analysis using either a Continuous Construction Test (for the Physical Work Test) or Continuous Efforts Test (for the Five Percent Safe Harbor).

Between 2013 and 2022, Treasury and the IRS repeatedly reaffirmed both methods of establishing BOC through a series of notices, and Congress enacted multiple statutes creating or extending credits with BOC deadlines without requiring any changes to the BOC framework. In late 2022, Treasury and the IRS confirmed that both methods remained available for the new Sections 45Y and 48E credits in Notice 2022-61, which provides that principles similar to those set forth in the IRS notices regarding the Continuity Requirement and the Continuity Safe Harbor apply for purposes of Sections 45Y and 48E, and that taxpayers may rely on the Continuity Safe Harbor provided the facility is placed in service no more than four calendar years after the calendar year during which construction began.

Observation: Treasury and the IRS reinforced this understanding in the preamble to the Section 45V final regulations, stating that “the beginning of construction date is an established, defined concept in tax law.” Treasury made that statement in adopting a BOC-based safe harbor, explaining that use of a BOC date “better supports the purpose of taxpayer certainty than a placed in service date,” suggesting BOC is a settled, cross-credit concept, rather than one limited to any particular credit or statutory provision.

Notice 2025-42

In response to the Executive Order, the issuance of Notice 2025-42 by Treasury and the IRS established the Physical Work Test as the exclusive method for most wind and most solar projects to demonstrate that construction began before the July 4, 2026, deadline. By making the Physical Work Test the sole method for most applicable wind and solar facilities, the Notice effectively removed the Continuous Efforts Test for wind and most solar facilities and provided that, unless the Continuity Safe Harbor applied, the continuity requirement must be met through a continuous program of construction based on the relevant facts and circumstances.

Observation: Between issuance of the Executive Order and publication of Notice 2025-42, developers and industry groups submitted extensive feedback to Treasury, warning that the industry had relied for years on the long-standing Five Percent Safe Harbor to secure financing and plan projects. Commenters also proposed more targeted alternatives to address potential manipulation, including limiting safe-harbor treatment for foreign-sourced equipment, rather than eliminating the Five Percent Safe Harbor wholesale.

In Notice 2025-42, Treasury and the IRS explain that the elimination of the Five Percent Safe Harbor was “necessary and appropriate” to “prevent taxpayers from circumventing the statutory credit termination date,” “prevent the artificial manipulation of eligibility,” and “ensure that a substantial portion of any applicable wind or solar facility . . . is built by the beginning of construction deadline.” The Notice did not directly address the numerous public comments received during the period between the Executive Order's issuance and the Notice's publication.

Case history

On December 18, 2025, the Oregon Environmental Council, the Natural Resources Defense Council (NRDC), tribal entities, and local governments filed a federal lawsuit in the US District Court for the District of Columbia. They challenged the guidance as "arbitrary and capricious" under the APA.

The court's ruling

On June 6, 2026, the court issued a comprehensive opinion addressing standing, jurisdictional issues (relying on the Anti-Injunction Act), and the merits of the APA challenge. The court held that Notice 2025-42 was arbitrary and capricious under the APA for three reasons.

- *Failure to articulate a reasoned basis for the policy change:* The court held that Notice 2025-42 marked a significant departure from the IRS's longstanding treatment of the Five Percent Safe Harbor as a valid method for satisfying BOC requirements. Notice 2025-42's stated rationale to prevent "circumventing the statutory credit termination date" and "artificial manipulation of eligibility" of the BOC requirements failed to explain how the Five Percent Safe Harbor enabled such conduct.
- *Failure to consider reliance interests and alternative policy options:* The court rejected Treasury's argument that reliance interests were limited because Sections 45Y and 48E were only recently enacted, focusing instead on the long history of the importance of the safe harbor to satisfying the BOC requirements. The court also found that the agency failed to address reasonable alternatives proposed by commenters, including enhanced reporting requirements, audit procedures, and restrictions on using purchases from prohibited foreign entities to satisfy the safe harbor. According to the court, the record did not show that "the agency diligently considered and rejected these possibilities and decided that its chosen path was the best way of addressing stockpiling concerns."
- *Failure to justify differential treatment:* Although the Sections 45Y and 48E credits are technology neutral, Notice 2025-42 singled out wind and large-scale solar projects without explaining why their earlier termination dates alone justified a different BOC standard. The court noted that "[m]oreover, nothing in the Notice or the administrative record explains why the concerns about stockpiling that the Defendants have identified in their briefing apply to wind and large-scale solar projects, but not to similarly situated clean energy projects based on other technologies."

The court vacated Notice 2025-42 in its entirety and remanded it to Treasury and the IRS, rejecting the government's request to limit relief to the plaintiffs.

Observation: The court's reasoning closely tracks the arguments advanced in the plaintiffs' briefs. The decision is also notable for what it does not address. The court adopted the perspective of the plaintiffs in framing the case primarily as an APA matter rather than as a traditional tax dispute. Whether subsequent appellate proceedings will reframe the issues remains to be seen.

Short-term win, long-term uncertainty

The court's decision, while significant, could be viewed as a starting point rather than a final resolution. Treasury and the IRS are widely expected to appeal. A stay of the court's ruling at some stage of the appellate process is also a meaningful possibility. The court itself acknowledged that, given the timing of the litigation, "there is 'almost zero chance' that the parties' appellate rights will not extend beyond the July 4 beginning of construction deadline."

With Notice 2025-42 vacated, taxpayers should reconsider the application of Notice 2013-29 and its successors, including Notice 2018-59, for establishing BOC under Sections 45Y and 48E. Notably, the court observed that Congress itself in the OBBBA codified the existing BOC framework as the standard for the new prohibited foreign entity (PFE) rules under Section 7701(a)(51), suggesting congressional acceptance of the existing approach.

Observation: With respect to the Continuity Requirement, vacating Notice 2025-42 would mean a return to the prior BOC guidance, including Notice 2021-41. As a result, taxpayers would again be able to satisfy the Continuity Requirement through either the Continuous Construction Test or the Continuous Efforts Test, regardless of whether BOC was established under the Physical Work Test or the Five Percent Safe Harbor. The Continuous Efforts Test, which includes the Continuous Construction Test, permits a broader range of activities to be considered and is generally viewed as easier to meet.

Next steps

In light of the court's ruling, taxpayers and developers of wind and solar projects should consider the following actions:

- *Reassess BOC strategy while preserving flexibility:* Projects redesigned or accelerated to satisfy the Physical Work Test in response to Notice 2025-42 may be able to revert to a Five Percent Safe Harbor approach, potentially reducing timing pressures. However, given the likelihood of an appeal, taxpayers should consider preserving flexibility by maintaining robust documentation supporting eligibility under both methods, including evidence to meet a facts and circumstances analysis of the Continuity Requirement.
- *Monitor for new guidance:* Treasury and the IRS must address the deficiencies identified by the court on remand. New guidance could re-impose limitations on the Five Percent Safe Harbor in a more reasoned manner, target stockpiling concerns directly, or take a different approach altogether.
- *Consider the PFE overlay:* Projects establishing BOC after December 31, 2025, still must navigate OBBBA's PFE rules, which appear to require the pre-Notice 2025-42 BOC framework.

The takeaway

The court's decision in *Oregon Environmental Council v. IRS* represents a significant development for the clean energy sector, restoring (at least for now) the long-standing dual-method framework for establishing BOC. While the vacatur provides welcome relief and renewed flexibility for wind and large-scale solar developers, significant uncertainty remains given the likelihood of an appeal and the possibility of new guidance from Treasury and the IRS on remand. Taxpayers should act promptly to assess the implications for their projects while remaining vigilant for further legal and regulatory developments in the months ahead.

PwC will continue to monitor developments in this area and provide updates as further guidance, judicial decisions, or legislative actions emerge.

Let's talk

For a deeper discussion of how this development might affect your business, please contact us.

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