

GIBSON DUNN



Tax Update

June 8, 2026

Federal Court Vacates IRS Guidance Limiting Grandfathering Safe Harbor for Wind and Solar Tax Credits

On June 6, 2026, a federal district court vacated IRS Notice 2025-42 in full, holding that the IRS acted arbitrarily and capriciously in eliminating the “Five Percent Safe Harbor” for certain tax credit-eligible wind and large solar projects seeking a longer completion deadline. Unless stayed or reversed on appeal, the decision restores that safe harbor for all such projects — though substantial uncertainty remains ahead of the OBBBA’s July 4, 2026 grandfathering deadline.

On June 6, 2026, the U.S. District Court for the District of Columbia issued its decision in *Oregon Environmental Council v. Internal Revenue Service* (the Decision), vacating Notice 2025-42 (the Notice) in full and remanding to the IRS.^[1] The court held that the Notice, which made “physical work of a significant nature” the only way most wind and solar projects could “begin construction” after 2024 before becoming subject to a more stringent statutory completion deadline, was arbitrary and capricious under the Administrative Procedure Act (the APA).

Background

Under current federal tax law, qualifying solar and wind energy facilities that begin construction after 2024 are eligible for either a 10-year production tax credit (rate based on kWh of electricity produced) or an investment tax credit (ranging from 30 to 70 percent of qualifying costs).^[2] The One Big Beautiful Bill Act (the OBBBA) accelerated the termination of these credits: For facilities on which construction begins after July 4, 2026, the facility must be placed in service by

December 31, 2027 to be eligible for credits.^[3] Projects that begin construction on or before July 4, 2026 (*i.e., in the next 27 days*), on the other hand, rely on IRS guidance indicating that a project's beginning of construction date will be respected as long as the facility is placed in service by the end of the fourth calendar year after the year in which construction began.

For over a decade, under IRS guidance interpreting prior identical statutory credit termination deadlines, a taxpayer could establish the "beginning of construction" either by performing physical work of a significant nature (the Physical Work Test) or by paying or incurring at least five percent of qualifying costs to construct the facility (the Five Percent Safe Harbor), and then placing the facility in service by the end of the fourth calendar year after the calendar year in which construction began.^[4]

In August 2025, implementing Executive Order 14315, the IRS issued the Notice, making the Physical Work Test the exclusive method for beginning construction on wind and solar facilities (except solar facilities of 1.5 MW or less) and eliminating the Five Percent Safe Harbor for those facilities, in each case, for purposes of the OBBBA's new credit termination deadline.^[5] In the Notice, the IRS stated that the purpose of the guidance was "to prevent taxpayers from circumventing the statutory credit termination date, prevent the artificial manipulation of eligibility for the [tax credits] for applicable wind and solar facilities, and ensure that a substantial portion of any applicable wind or solar facility not subject to the credit termination date is built by the beginning of construction deadline." The practical impact of the Notice was that it made it more challenging for wind or solar facilities to establish that construction had begun, therefore making it more challenging to benefit from the extended placed in service deadline.

The Court's Decision

After resolving the government's threshold objections as to jurisdictional and standing matters, holding that five of the seven plaintiffs had standing, the court reached the merits.

On the merits, the court held the Notice arbitrary and capricious. An agency reversing a longstanding position must acknowledge the change, weigh the serious reliance interests its prior policy created, and explain its reasons. The court found the Notice's lone explanatory paragraph inadequate: it did not explain how Five Percent Safe Harbor facilities were "circumventing" the statute, why the IRS rejected the narrower anti-abuse alternatives commenters proposed (such as barring safe-harbor purchases from prohibited foreign entities), or why wind and large solar facilities were singled out.

The court ordered the ordinary APA remedy — vacatur in full and remand to the IRS — declining both to remand without vacating and to limit relief to the plaintiffs, because only universal vacatur could fully redress injuries flowing from the Notice's effect on third-party developers.

What This Means

- **The Five Percent Safe Harbor for the OBBBA's July 4, 2026 deadline is restored — if the IRS agrees.** With the Notice vacated, the pre-Notice beginning-of-construction guidance, including the Five Percent Safe Harbor, again governs wind and large solar (small solar of 1.5 MW or less was never affected). But a government appeal and a stay request are likely, the court warned that appellate review will probably outlast the July 4,

2026 deadline, and the IRS may re-issue guidance on remand, meaning that market participants must plan for continued uncertainty. Absent immediate IRS acquiescence to the Decision, the resulting uncertainty means the availability of the Five Percent Safe Harbor is likely of little practical use.

- **Document both methods.** Any developers considering relying on the Five Percent Safe Harbor should also document satisfaction of the Physical Work Test, so eligibility does not turn on which rule ultimately prevails.

[1] *Oregon Env't Council v. IRS*, No. 1:25-cv-04400-CKK (D.D.C. June 6, 2026). All references to the "IRS" and the "Treasury" are to the U.S. Internal Revenue Service and the U.S. Department of the Treasury, respectively.

[2] Facilities for which construction begins before 2025 are eligible for different (albeit similar) credits that are not affected by the Notice.

[3] Pub. L. No. 119-21, §§ 70512–70513 (2025).

[4] See Notice 2013-29 and its successor notices (each method subject to a continuity requirement). The IRS completion deadlines are longer for certain more complex facilities and facilities constructed during the Covid-19 pandemic.

[5] Notice 2025-42, 2025-36 I.R.B. 351; Exec. Order No. 14315, 90 Fed. Reg. 30821 (July 7, 2025). Our prior alert on the Notice can be found [here](#).

The following Gibson Dunn lawyers prepared this update: Josiah Bethards, Michael Q. Cannon, and Matt Donnelly.

Gibson Dunn lawyers are available to assist in addressing any questions you may have regarding this decision. To learn more about these issues or discuss how they might impact your business, please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any member of the firm's [Tax](#) and [Tax Controversy and Litigation](#) practice groups:

Tax:

[Dora Arash](#) – Los Angeles (+1 213.229.7134, darash@gibsondunn.com)

[Michael Q. Cannon](#) – Dallas (+1 214.698.3232, mcannon@gibsondunn.com)

[Matt Donnelly](#) – New York/Washington, D.C. (+1 212.351.5303, mjdonnelly@gibsondunn.com)

[Evan M. Gusler](#) – New York (+1 212.351.2445, egusler@gibsondunn.com)

[James Jennings](#) – New York (+1 212.351.3967, jjennings@gibsondunn.com)

[Kathryn A. Kelly](#) – New York (+1 212.351.3876, kkelly@gibsondunn.com)

[Rachel D. Kleinberg](#) – Palo Alto (+1 650.849.5207, rkleinberg@gibsondunn.com)

[Brian W. Kniesly](#) – New York (+1 212.351.2379, bkniesly@gibsondunn.com)

[Pamela Lawrence Endreny](#) – Co-Chair, New York (+1 212.351.2474,

pendreny@gibsondunn.com)

[Gregory V. Nelson](mailto:gnelson@gibsondunn.com) – Houston (+1 346.718.6750, gnelson@gibsondunn.com)

[Jennifer Sabin](mailto:jsabin@gibsondunn.com) – New York (+1 212.351.5208, jsabin@gibsondunn.com)

[Eric B. Sloan](mailto:esloan@gibsondunn.com) – Co-Chair, New York/Washington, D.C. (+1 212.351.2340, esloan@gibsondunn.com)

[Edward S. Wei](mailto:eweiz@gibsondunn.com) – New York (+1 212.351.3925, eweiz@gibsondunn.com)

[Lorna Wilson](mailto:lwilson@gibsondunn.com) – Los Angeles (+1 213.229.7547, lwilson@gibsondunn.com)

Tax Controversy and Litigation:

[Saul Mezei](mailto:smezei@gibsondunn.com) – Washington, D.C. (+1 202.955.8693, smezei@gibsondunn.com)

[Sanford W. Stark](mailto:ss Stark@gibsondunn.com) – Chair, Washington, D.C. (+1 202.887.3650, ss Stark@gibsondunn.com)

[C. Terrell Ussing](mailto:tussing@gibsondunn.com) – Washington, D.C. (+1 202.887.3612, tussing@gibsondunn.com)

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