Simpson Thacher

Memorandum

President Trump Signs Legislation Enacting Phased Elimination of Federal Tax Credits for New Clean Energy Projects; Directs Treasury to "Strictly Enforce" Credit Termination for Solar and Wind Facilities

July 8, 2025

On July 3, 2025, the U.S. Congress passed and, on July 4, 2025, President Trump promptly signed into law, the "One Big Beautiful Bill Act" (the "Act"), making sweeping changes to U.S. federal income tax credits provided to the clean energy sector that were enacted under the Biden administration as part of the Inflation Reduction Act of 2022 (the "IRA"). On July 7, 2025, President Trump then issued an executive order (the "Executive Order") relating to the implementation of such changes ("Ending Market Distorting Subsidies for Unreliable, Foreign Controlled Energy Sources").

Key features of the Act include:

- No retroactive clawback of tax credits for projects that are currently operational.
- No expected impact on projects that began construction—as determined under Internal Revenue Service ("IRS") guidance—prior to the Act's date of enactment, subject to the caveat that it is uncertain whether the Executive Order (discussed further below) will modify this guidance retroactively.
- The date on which a project "begins construction" is significant for determining continued credit eligibility:
  - The U.S. federal production tax credit ("PTC") and investment tax credit ("ITC") for solar and wind projects that begin construction after July 4, 2026 are eliminated unless the project is "placed in service" by December 31, 2027.
  - The PTC and ITC for battery, hydropower, geothermal, and other electricity-generating projects with zero lifecycle greenhouse gas emissions will remain eligible for the full amount of credits as long as they begin construction before 2034.
  - The PTC and ITC are unavailable to projects that begin construction after December 31, 2025 and receive material assistance (including the provision of certain equipment) from "foreign entities of concern" ("FEOCs") and other "prohibited foreign entities." FEOCs and other prohibited foreign entities will also become ineligible to claim the PTC, ITC, and several other tax credits.
  - Projects that began construction prior to 2025 are not affected by the Act, as project sponsors may elect to rely on the pre-IRA versions of the PTC and ITC under Sections 45 and 48 of the Internal Revenue Code (the "Code").

- Any entitlement to bonus credits (or "adders") for qualifying projects is preserved, including the "energy community" adder and the "domestic content" adder. Qualifying "energy communities" for nuclear projects are expanded.
- Transferability of tax credits has been retained (subject to new limitations on transfers to certain foreign entities).
- No penalty excise tax on solar and wind projects that receive material assistance from FEOCs and other prohibited foreign entities, which had been included in an earlier Senate draft of the legislation.

The final Act reflects a compromise between Republican legislators in the House of Representatives, who favored a rapid sunset for most of these tax credits, and in the Senate, who had favored a more gradual phase-out of the credits, and brings some measure of stability to the clean energy generation industry after months of uncertainty.

However, the Executive Order appears to reintroduce uncertainty for solar and wind project developers regarding whether their projects will continue to be eligible for tax credits. The Executive Order directs the Department of the Treasury ("Treasury") to review the long-established safe harbor rules for determining whether a solar or wind project has "begun construction" for U.S. federal income tax purposes, creating potential uncertainty whether projects will be able to meet any of the key start-of-construction deadlines referenced above. In addition, while beyond the scope of this alert, the Executive Order also directs the Department of the Interior to review and revise its existing regulations, guidance, policies and practices to eliminate any preferences for wind and solar facilities relative to dispatchable energy sources.

Changes to the PTC & ITC

PRIOR LAW

The IRA provided for a 10-year PTC for certain facilities that generate electricity with zero net greenhouse gas emissions, which can include both wind and solar energy facilities. The IRA also provided for an ITC equal to a percentage of a taxpayer's investment in such facilities, as well as in property used for the storage of electricity, hydrogen, or thermal energy ("energy storage technology" or "EST"). Under the IRA, the PTC and the ITC were each subject to a gradual phase-out that would begin for facilities and EST that started construction two calendar years after the year in which annual U.S. greenhouse gas emissions from the production of electricity were 25% or less of their 2022 level (but in no case earlier than 2032).

In addition, in lieu of claiming the PTC or the ITC, the IRA permitted certain taxpayers to transfer the credits by selling them to another taxpayer in exchange for a payment in cash or cash equivalents.

ACCELERATED SUNSET FOR SOLAR & WIND; PHASE-OUT FOR OTHER PROJECTS

The Act creates a two-track repeal of the PTC and ITC: one schedule for solar and wind projects and a separate schedule for EST (including EST placed in service at a solar or wind facility) and clean electricity generation projects that rely on other technologies (*e.g.*, hydropower, geothermal, and nuclear). The Act eliminates the PTC and the ITC for solar and wind projects that begin construction more than 12 months after its date of enactment (*i.e.*, after July 4, 2026) if those projects are not "placed in service" by December 31, 2027. Thus, solar and wind projects that do not qualify for the "start-of-construction" safe harbor will confront the possibility that unexpected or unavoidable delays in construction may cause them to miss the December 31, 2027 placed-in-service deadline and lose credit eligibility. As discussed below, the Executive Order raises numerous questions regarding how Treasury and the IRS will apply the start-of-construction safe harbor.

For EST and other clean electricity generation projects, the Act phases out the PTC and the ITC according to the following schedule:

Phase-out Schedule for EST & Non-Solar & Wind Electricity-Generating Projects

If construction begins in…	…the percentage of the credit allowed is:
2033 or earlier	100%
2034	75%
2035	50%
2036 or later	Credit Eliminated

The Act restores the ITC eligibility of qualified fuel cell property that begins construction after 2025. Under the IRA, qualified fuel cell property was required to have begun construction prior to 2025 in order to be eligible for the ITC. Additionally, taxpayers are not required to comply with the IRA's "prevailing wage and apprenticeship" requirements with respect to the construction, alteration, and repair of qualified fuel cell property in order to claim the maximum ITC. However, qualified fuel cell property is not eligible for any bonus credits (or "adders"). The ITC with respect to qualified fuel cell property is subject to the phase-out schedule described in the table above.

The Act eliminates, beginning in 2026, the PTC and ITC for residential solar leases, though this change is expected to practically impact only a small number of states whose laws impede rooftop solar companies from directly entering into power purchase agreements with retail customers (and where leasing is therefore more prevalent as an alternative). This prohibition also applies to residential wind leases.

START OF CONSTRUCTION AND THE EXECUTIVE ORDER

The Executive Order directs Treasury to, by August 18, 2025, issue such new and revised guidance for determining a project's start-of-construction date as it deems necessary to enforce the Act's sunset of the PTC and ITC for solar and wind projects. Under the IRS's existing guidance (the "Start-of-Construction Guidance"), the start-of-construction date for a project can be established by (1) beginning physical construction on site or (2) incurring 5% of expenditures with respect to a project, provided that the project is ultimately placed in service (in most cases) by the end of the fourth calendar year after the deemed start-of-construction date. Additionally, the Start-of-Construction Guidance does not require that the taxpayer be the person that actually started construction on the project and allows, in some circumstances, for the transfer of project components with "safe-harbored" start-of-construction dates between different taxpayers, in particular between related entities.

It is uncertain how Treasury will interpret or implement the Executive Order, but under the Executive Order the Secretary of the Treasury is directed to issue new and revised guidance "preventing the artificial acceleration or manipulation of eligibility" and "restricting the use of broad safe harbors unless a substantial portion of a subject facility has been built." Consistent with this mandate, relative to the existing Start-of-Construction Guidance, the revised guidance could require that construction have reached a more advanced stage or that a higher percentage of overall expenditures have been incurred to establish a start-of-construction date, shorten the four-year placed-in-service requirement, and/or impose new limitations on the ability of taxpayers to transfer "safe-harbored" project components between themselves. Any such changes could materially impair the ability of new solar and wind projects to "begin construction" in time to qualify for the PTC or the ITC without the need to satisfy the December 31, 2027 placed-in-service deadline.

In addition, the Executive Order directs the Department of the Interior, also by August 18, 2025, to eliminate any preferences in its existing regulations, guidance, policies, and practices that favor solar or wind projects over dispatchable energy sources. Such actions could have the effect of protracting the time it takes for solar and wind projects to receive permits or other regulatory approvals and thus delay their progress towards a state of having "begun construction."

BONUS CREDITS PRESERVED

Under the Act, any entitlement to bonus credits (or "adders") for qualifying projects is preserved, including the "energy community" adder and the "domestic content" adder. Additionally, the Act expands the types of qualifying "energy communities" specifically for certain nuclear projects.

TRANSFERABILITY GENERALLY PRESERVED

The Act preserves the ability of taxpayers to sell PTCs and ITCs, as well as the tax credits discussed in the following section. However, as discussed later in this Alert, for certain tax credits, including the PTC and ITC, a "prohibited foreign entity" (as defined below) would be an ineligible credit purchaser. This limitation does not affect the transfer of PTCs and ITCs with respect to projects that began construction prior to 2025 and qualify for the pre-IRA versions of the credits under Sections 45 and 48 of the Internal Revenue Code (the "Code").

Changes to Other Tax Credits

EXTENSION FOR CLEAN TRANSPORTATION FUELS

Under the IRA, a clean fuel production tax credit under Code Section 45Z (the "45Z credit") was available for sales of clean transportation fuels, including sustainable aviation fuel, that occur between 2025 and 2027. A preferential credit amount applied to sales of sustainable aviation fuel that was 75% greater than the standard credit amount that applied to sales of other clean transportation fuels.

The Act extends the 45Z credit for sales of sustainable aviation fuel and other clean transportation fuels through 2029, but imposes a new requirement that fuel produced after 2025 be "exclusively" derived from feedstock produced or grown in the United States, Mexico, or Canada in order to qualify for the credit. Additionally, sales of sustainable aviation fuel produced after 2025 will no longer be eligible for the preferential credit amount and will instead receive the same credit amount as sales of other clean transportation fuels. The Act also amends the criteria for the lifecycle greenhouse gas emissions analysis used to determine eligibility for the 45Z credit in a manner expected to be more generous to fuel producers, but clarifies that the emissions rate determined cannot be negative.

The Act also eliminates the current federal excise tax credit for sustainable aviation fuel, effective for sales occurring after September 30, 2025.

PHASE-OUT OR ELIMINATION OF OTHER CREDITS

The Act accelerates the sunset of several other credits relating to electric vehicles ("EV") and their related infrastructure, including relative to the first draft of the legislation. The Code Section 30D credit (for buyers of new clean vehicles) and the Code Section 45W credit (for buyers of commercial clean vehicles) is eliminated for vehicles purchased after September 30, 2025. The Code Section 30C credit (for installation of EV charging stations) is eliminated for property placed in service after June 30, 2026.

The Act phases out the advanced manufacturing production credit under Code Section 45X for the production of "applicable critical minerals" at a rate of 25% per year beginning in 2031. Sales of other "eligible components" will remain eligible for the Code Section 45X credit according to the existing phase-out schedule under the IRA, with the exception of wind energy components, for which the credit is eliminated for sales occurring after 2027.

The Act imposes new limits on the current ability of a taxpayer's ability to "stack" the Code Section 45X credit by selling an "eligible component" to a related taxpayer which then incorporates it as a component of a different "eligible component" that is sold to an unrelated party. Effective for sales occurring after December 31, 2026, a taxpayer will be permitted to claim the Code Section 45X credit with respect to a primary component that is incorporated into a secondary component that is sold to an unrelated party only if the secondary component is produced in the same manufacturing facility as the primary component and at least 65% of the taxpayer's total direct material costs to produce the secondary component are attributable to primary components that are mined, produced, or manufactured in the United States.

The final Act accelerates the sunset of the production and investment tax credits for clean hydrogen facilities for projects that begin construction after 2027. This sunset date is two years later than in earlier drafts of the legislation, under which credits for clean hydrogen projects would have been cut off for projects beginning construction after 2025.

Restrictions on Transactions with Foreign Entities

The Act includes provisions intended to address the direct and indirect reliance of the clean energy industry on the Chinese supply chain by prohibiting taxpayers that engage in certain transactions with foreign entities from claiming new tax credits. These prohibitions fall into two categories: (1) restrictions related to ownership, funding and services (the “prohibited foreign entity” restrictions) and (2) restrictions related to procurement and construction (the “material assistance” restrictions). These new restrictions will not become effective until after 2025, and the Executive Order directs the Secretary of the Treasury to take such “prompt” action, by August 18, 2025, as the Secretary deems appropriate and consistent with applicable law to implement the restrictions.

PROHIBITED FOREIGN ENTITIES

For taxable years beginning after the Act’s date of enactment (*i.e.*, starting in 2026, for calendar-year taxpayers), a taxpayer will be ineligible to claim the PTC or ITC if it is a “specified foreign entity” or a “foreign-influenced entity” (together, “prohibited foreign entities”). “Specified foreign entities” generally include FEOCs (and certain other foreign companies identified as problematic under federal statutes) as well as the governments of China, Iran, North Korea, and Russia, citizens of and entities organized in those nations, and any other entity that is controlled by any of the foregoing. “Control” in this context generally means greater than 50% equity ownership, but the Act loosens this requirement with respect to publicly traded entities and certain subsidiaries of publicly traded entities by limiting the types of specified foreign entities whose equity ownership would count towards this 50% ownership threshold.

Two alternative tests apply to determine whether an entity is a “foreign-influenced entity” in any given taxable year. Under the first test, a taxpayer is a foreign-influenced entity if, in the relevant taxable year, a specified foreign entity has the authority to appoint a board member or executive-level officer or owns 25% or more of the equity of the taxpayer, or if a combination of specified foreign entities own 40% or more of the equity of the taxpayer in the aggregate. An entity is also considered to be a “foreign-influenced entity” if 15% or more of the total debt of the entity has been issued, in the aggregate, to one or more specified foreign entities. A more lenient version of this test applies to publicly traded entities and certain subsidiaries of publicly traded entities, including that only debt originally issued to a specified foreign entity counts towards the 15% threshold.

Under the second test, a taxpayer is a foreign-influenced entity if, during the preceding taxable year, it made a payment to a specified foreign entity pursuant to a contract or other agreement that entitles the specified foreign entity to exercise “effective control” over a project. The Act contains interim guidance as to the meaning of “effective control,” but delegates the ultimate definition of that term to the Treasury Department to clarify by regulation.

The prohibited foreign entity restrictions also apply to the Code Section 45X credit and the carbon sequestration credit under Code Section 45Q. The restrictions apply to the 45Z credit and the nuclear power credit under Code Section 45U on a staggered basis, with such restrictions taking effect for specified foreign entities in taxable years beginning after the Act’s date of enactment (*i.e.*, starting in 2026, for calendar-year taxpayers) and for foreign-influenced entities in taxable years beginning more than two years after the Act’s date of enactment (*i.e.*, starting in 2028, for calendar-year taxpayers). Additionally, in taxable years beginning after the Act’s date of enactment (*i.e.*, starting in 2026, for calendar-year taxpayers), prohibited foreign entities will be ineligible to purchase any of these credits, as well as PTCs and ITCs (provided that, with respect to the 45Z credit and the nuclear power credit under Code Section 45U, a foreign-influenced entity could continue to purchase such credits until the staggered effective date mentioned above).

None of these prohibited foreign entity restrictions apply to the pre-IRA versions of the PTC and ITC under Code Sections 45 and 48 that apply to projects that began construction prior to 2025.

MATERIAL ASSISTANCE

The material assistance restrictions apply only to projects that begin construction after December 31, 2025. Under these rules, no tax credit is allowed (to any investor in such a project) if the project receives “material assistance from a prohibited foreign entity.”

Whether a project has received material assistance from a foreign entity is determined based on its “material assistance cost ratio,” which is based on the taxpayer’s direct input costs attributable to manufactured products that are not produced by prohibited foreign entities, relative to the taxpayer’s total direct input costs attributable to all manufactured products included in the project. If the ratio does not meet a threshold level (which will gradually step up each year from 2025-2030), the project will be ineligible for a PTC or ITC. The material assistance cost ratio thresholds that would apply to EST would be higher than those that apply to electricity-generating projects. At the election of the taxpayer, the cost of manufactured products acquired pursuant to a binding written contract entered into prior to June 16, 2025 and placed in service prior to January 1, 2030 may be excluded from the calculation of the material assistance cost ratio.

For the purposes of determining the material assistance cost ratio, taxpayers are be permitted to rely on certifications provided by suppliers that a given manufactured product was not produced by a prohibited foreign entity. To enforce compliance, the Act imposes new penalties on suppliers that provide false or inaccurate certifications after December 31, 2025. The statute of limitations for assessment of penalties with respect to the material assistance rules will be six years.

In addition to the PTC and the ITC, the material assistance restrictions also apply to the Code Section 45X advanced manufacturing production credit, with the material assistance cost ratio in such case being based on direct material costs for the production of the relevant "eligible component" (subject to the same election described above to exclude the cost of certain constituent materials and subcomponents acquired pursuant to a binding written contract).

The Act explicitly confirms that the Start-of-Construction Guidance will be used when applying the material assistance restrictions. However, it is uncertain whether any revisions to the Start-of-Construction Guidance for solar and wind projects pursuant to the Executive Order would also apply for the purposes of the material assistance restrictions.

FUEL SOURCING FOR NUCLEAR PROJECTS

Under the Act, a nuclear project generally will be ineligible for the production tax credit under Code Section 45U in any taxable year beginning after 2027 if it uses any fuel produced in China, Iran, North Korea, or Russia or by an entity organized in one of those countries. The IRA had contained no such limitation on fuel sourcing to qualify for the credit.

Observations

IMPLICATIONS FOR EXISTING PROJECTS

Because the Act phases out the PTC and ITC on a prospective basis, projects that are currently operational or that have validly begun construction will remain eligible for the PTC and the ITC as well as for the credit transferability provisions of the IRA. However, unless a project began construction before 2025 and qualifies for the pre-IRA PTC and ITC (under Code Sections 45 and 48), owners of the project will still be subject to the Act's new prohibited foreign entity restrictions and could become ineligible to claim the tax credits in future taxable years after such restrictions take effect.

IMPLICATIONS FOR NEW PROJECTS

The accelerated sunset of the PTC and ITC for solar and wind projects under the Act is a setback for these industries and may impact development of many of these projects. Until Treasury releases revised Start-of-Construction Guidance pursuant to the Executive Order, developers and investors face uncertainty as to whether a solar or wind project will be able to "begin construction" by the July 4, 2026 grandfathering cutoff date in order to qualify for the exemption from the December 31, 2027 placed-in-service requirement. In the case of large (*e.g.*, utility-scale) projects, due to the relatively short runway until the placed-in-service deadline on December 31, 2027, it may effectively be impossible for such projects to continue to qualify for the PTC or the ITC if they do not begin construction within the grandfathering period. Smaller-scale projects, such as residential solar, may have a more realistic chance of meeting the placed-in-service deadline if they do not qualify for grandfathered status (*i.e.*, validly begin construction by July 4, 2026).

Another unanswered question is whether the same Start-of-Construction Guidance that will apply to solar and wind projects for the purpose of determining PTC or ITC eligibility will also apply for the purpose of determining whether the Act's new material assistance restrictions apply to a project and, if so, what the applicable material assistance cost ratio threshold will be. Ideally, this will also be clarified in any guidance issued by Treasury pursuant to the Act or the Executive Order.

Although the more gradual credit phase-out schedule for EST and other clean electricity generation projects will not take effect until 2034, such projects will be required to comply with the material assistance restrictions if they do not begin construction on or before December 31, 2025. Although the Executive Order applies only with respect to solar and wind projects, it remains uncertain whether any issued guidance modifying the Start-of-Construction Guidance could apply, in whole or in part, to such other projects as well. Project owners are advised to speak to their tax advisors regarding how these new rules may apply to them.

We Can Help

For further information regarding this Alert, the Act, the Executive Order, or their implications for the clean energy sector and its investors, please speak to your regular contact in the Simpson Thacher Tax Department or contact one of the following:

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