HOW FOREIGN ENTITY OF CONCERN RESTRICTIONS WILL RESHAPE CLEAN ENERGY TAX CREDITS

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Holland & Knight

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Meet Our Presenters



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- The President signed the One Big Beautiful Bill Act (OB3) on July 4th
- In addition to curtailing certain energy tax credits, the OB3 included several foreign entity of concern (FEOC) restrictions
- Executive Order dated July 8th directed Treasury to act within 45 days to implement the new FEOC restrictions
- Under OB3 these FEOC restrictions apply to most energy tax credits:
  - Investment Tax Credit – Section and 48E
  - Production Tax Credit – Section 45Y
  - Advanced Manufacturing Tax Credit – Section 45X
  - Zero-Emission Nuclear Power Production – Section 45U
  - Clean Fuel Production Credit – Section 45Z
  - Credit for Carbon Oxide Sequestration – Section 45Q

Application of FEOC Restrictions

	Txp cannot be a Specified Foreign Entity (SFE)	Txp cannot be a Foreign Influenced Entity (FIE)	There can be no "material assistance" from a Prohibited Foreign Entity (PFE)
45Y, 48E	Tax years after enactment	Tax years beginning after enactment	Facilities that begin construction after 12/31/2025
45X		Tax years beginning after enactment	Tax years beginning after enactment
45U, 45Z, 45Q		Tax years beginning two years after enactment and determined without regard to "Payment Rule"	Not applicable

A PFE = Both SFE and FIE

FEOC Restrictions – Testing Dates

- Taxpayer cannot claim credits if a Specified Foreign Entity (SFE) or a Foreign Influenced Entity (FIE)
  - Tested the last day of the taxable year
  - Initial year exception
    - A limited test highlighted by dashed box in next slide is tested the first day of the taxable year.
  - Example of calendar year taxpayer testing for the year 2026:



Question One: Who is considered a Specified Foreign Entity (SFE)?

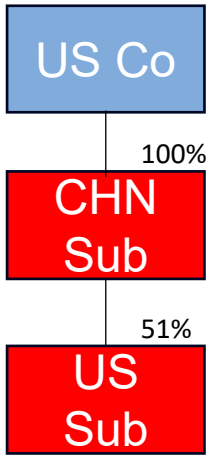
1. Meets certain definitions as included in the William Thornberry National Defense Authorization Act (NDAA) for fiscal year (FY) 2021:
   - designated as a foreign terrorist organization by the U.S. Secretary of State
   - included on the list of specially designated nationals and blocked persons maintained by the Treasury Department's Office of Foreign Assets Control (OFAC)
   - alleged by the U.S. Attorney General to have been involved in activities for which a conviction was obtained
   - determined by the U.S. Secretary of Commerce to be engaged in unauthorized conduct that is detrimental to national security or foreign policy
2. Identified as a Chinese military company
3. Is included on the Uyghur Forced Labor Prevention Act (UFLPA) Entity List
4. Is specified under Section 154(b) under the NDAA of FY 2024

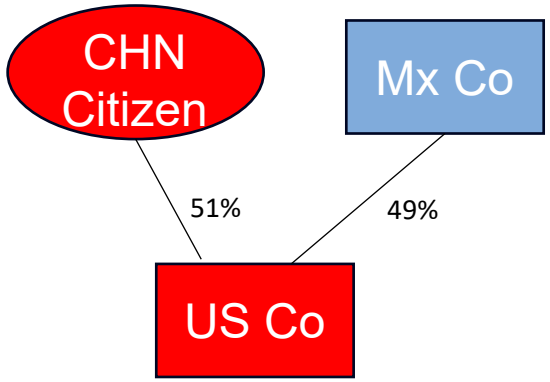
OR…

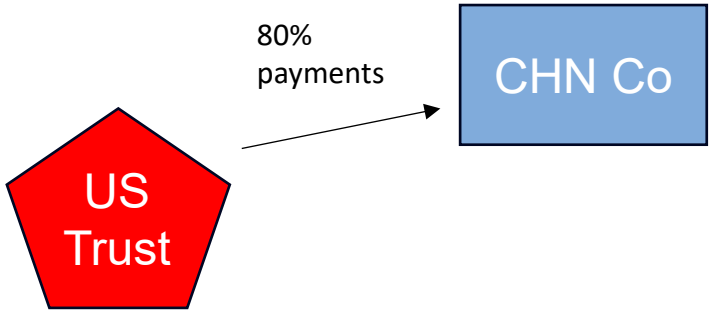
5. Is a Foreign Controlled Entity
   - The government of a covered nation, an agency or instrumentality of a covered nation, a citizen or national of a covered nation, an entity or business unit incorporated or organized or having its principal place of business in a covered nation; or
   - Is any entity "controlled" by such
     - “Control" = greater than 50 percent vote or value of stock of corporation or 50 percent capital interest or beneficial interest.
     - Upwards attribution is considered.

A covered nation =
- the Democratic People's Republic of North Korea;
- the People's Republic of China;
- the Russian Federation; and
- the Islamic Republic of Iran

Three examples of Specified Foreign Entities:

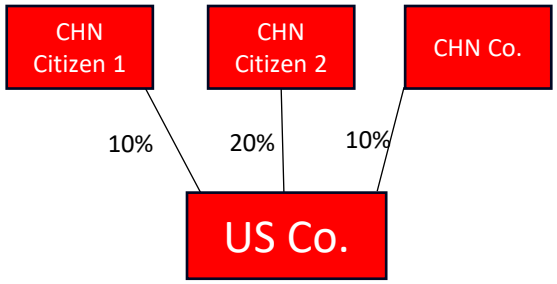






Question Two: Who is considered a Foreign Influenced Entity (FIE)?

1. An SFE has direct authority to appoint a covered officer;
2. A single SFE owns 25 percent or more of such entity;
3. More than one SFE owns, in the aggregate, 40 percent or more of such entity; or
4. At least 15 percent of debt of the entity was issued to one or more SFEs;



OR...

5. A payment was made to a SFE
   - Requires consideration of payments made in previous taxable year to a SFE, e.g. if considering availability of TY 2026, need to look at payments made in TY 2025.
   - Asks whether such payments were made pursuant to a contract, agreement or other arrangement that provided SFE with effective control.
     - Effective control to be defined in guidance, but in interim means authority over key aspects of production of eligible components, energy generation or energy storage.
     - Special rule for licensing agreements: Includes when such agreement allows an SFE to source items (components, subcomponents, critical minerals), direct the operation, utilize intellectual property, or receive royalties or any license agreement entered into or modified after July 4, 2025.
       - Only exception is for bona fide purchase of intellectual property.

Special Rules for Publicly Traded Entities

When are Publicly Traded Entities not considered Foreign-Controlled Entities (a type of SFEs)?

Foreign-Controlled Entity or Not?	
Not a Foreign-Controlled Entity	Securities are regularly traded on certain exchanges: • National securities exchange registered with SEC (*e.g.*, NYSE), • The national market system established under Sec. 11A of SEC Act, OR • Foreign market or exchange satisfying Treas. Reg. 1.1296-2(c)(1)(ii) (unless market or exchange is incorporated, organized under the laws of, or has its principal place of business in a covered nation (*e.g.*, China)),
Unless…	• If *controlled* by 1 or more SFEs or 1 or more FCEs that are required to report beneficial ownership under SEC Rule 13d-3

When are Publicly Traded Entities not counted as Foreign-Influenced Entities?

Foreign-Influenced Entity or Not?	
Not a Foreign-Influenced Entity	• Securities are regularly traded on certain exchanges (*i.e.*, on a registered national securities exchange, the national market system, or a foreign market or exchange satisfying Treas. Reg. 1.1296-2(c)(1)(ii)) (unless such market or exchange is incorporated, organized under the laws of, or has its principal place of business in a covered nation (e.g., China)), **OR** • At least 80% of equity securities of such entity are owned *directly or indirectly* by another entity whose securities are regularly traded on those markets or exchanges

Unless…	• During the taxable year,
	  ◦ SFE has authority to appoint a covered officer (e.g., member of board of directors, executive-level officer)
	  ◦ Single SFE required to report beneficial ownership under SEC Rule 13d-3 (or equivalent rules) owns 25% of the entity
	  ◦ Multiple SFEs required to report beneficial ownership under SEC Rule 13d-3 own, in the aggregate, 40% of the entity, **OR**
	• Issued debt, as part of original issuance, in excess of 15% of its publicly-traded debt to one or more SFEs

Material Assistance Rules

(Sections 45Y/48E/45X ONLY)

Sections 48E and 45Y – Applicable to projects BOC after 12/31/2025

1. Determine whether the manufacturer of each manufactured product component* is a Prohibited Foreign Entity, and
2. Ensure that the required applicable percentage is sourced from entities which are not Prohibited Foreign Entities.
3. Under statute, based on direct costs to taxpayer.
4. Safe harbor guidance forthcoming, prior to such guidance taxpayers can rely on IRS Notice 2025-08 and certifications from suppliers.
5. Exception available for manufactured product components acquired under existing contracts.

Example of Material Assistance Calculation:

Total direct costs to the taxpayer attributable to all manufactured products (including components) which are incorporated into the facility upon completion of construction

minus

Total direct costs to the taxpayer attributable to all manufactured products (including components) which are incorporated into the facility upon completion of construction, and mined, produced, or manufactured by a prohibited foreign entity

divided by

Total direct costs to the taxpayer attributable to all manufactured products (including components) which are incorporated into the facility upon completion of construction

=

?%

Applicable percentage for qualified facility:

BOC in 2026 – 40%
BOC in 2027 – 45%
BOC in 2028 – 50%

(Energy Storage – 55%,60%,65%)

Section 45X – Applicable tax years after enactment

- Looks to direct material costs to Section 45X taxpayer.
  - This could include anything, such a subcomponents, taxpayer acquires to produce the eligible component.
  - Taxpayers can rely on certifications from suppliers.

- Requires that the applicable percentage of the materials is sourced from entities which are not Prohibited Foreign Entities.
  - For example, for an inverter sold in 2026, the applicable percentage is 50%

Example of Material Assistance Calculation:

With respect to an eligible component, the total direct material costs that are paid or incurred by the taxpayer for production of such eligible component

minus

With respect to an eligible component, the total direct material costs that are paid or incurred by the taxpayer for production of such eligible component that are mined, produced, or manufactured by a prohibited foreign entity

=

?%

divided by

With respect to an eligible component, the total direct material costs that are paid or incurred by the taxpayer for production of such eligible component

Applicable percentage for inverters:
Sold in 2026 – 50%
Sold in 2027 – 55%
Sold in 2028 – 60%

Questions?