

Treasury and IRS Issue Interim Guidance on Prohibited Foreign Entity Rules with New Safe Harbors Under Notice 2026-15

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On February 12, 2026, the Department of the Treasury and the Internal Revenue Service released Notice 2026-15, the first substantive regulatory action implementing the prohibited foreign entity ("PFE") provisions enacted by the One, Big, Beautiful Bill Act ("OBBBA") on July 4, 2025. The Notice provides interim guidance on restrictions to the Section 45Y clean electricity production credit, the Section 48E clean electricity investment credit, and the Section 45X advanced manufacturing production credit, with respect to sourcing from a PFE. It establishes temporary safe harbors and reliance rules for determining whether a facility, energy storage technology ("EST"), or eligible component includes "material assistance from a PFE," while previewing how Treasury and the IRS intend to approach related concepts, including effective control, in forthcoming proposed regulations. Unlike the domestic content bonus credit, which merely offered an incremental adder, these rules are binary: a facility that fails is ineligible for the tech-neutral ITC or PTC entirely with potentially devastating consequences for project capital stack.

The Statutory Framework

The OBBBA added new Sections 45Y(b)(1)(E), 48E(b)(6) and (c)(3), and 45X(c)(1)(C) to the Code, providing that the terms "qualified facility," "energy storage technology," and "eligible component" do not include items that incorporate material assistance from a PFE. The OBBBA simultaneously amended Section 7701 to add new paragraphs (a)(51) and (a)(52), defining a "prohibited foreign entity" and "material assistance from a prohibited foreign entity," respectively.

Under Section 7701(a)(52), "material assistance from a PFE" is present when a facility's, EST's, or eligible component's material assistance cost ratio ("MACR") falls below the applicable threshold percentage. The threshold percentages phase in over time based on the calendar year during which construction of a qualified facility or EST begins (for Sections 45Y and 48E) or the calendar year during which an eligible component is sold (for Section 45X). For example, a qualified facility beginning construction in calendar year 2026 must achieve a Clean Electricity MACR of not less than 40% (for qualified facilities) or 55% (for ESTs), and a solar energy component sold during calendar year 2026 must achieve an Eligible Component MACR of not less than 50%.

Calculating the MACR: A Two-Track System

Notice 2026-15 establishes a detailed framework for calculating the MACR, distinguishing between two tracks: the "Clean Electricity MACR" (for qualified facilities and ESTs under Sections 45Y and 48E) and the "Eligible Component MACR" (for Section 45X eligible components).

Clean Electricity MACR

For qualified facilities and ESTs, the Clean Electricity MACR equals the taxpayer's total direct costs attributable to all manufactured products ("MPs") and manufactured product components ("MPCs") incorporated into the facility or EST, minus the total direct costs attributable to MPs and MPCs that were mined, produced, or manufactured by a PFE, divided by the total direct costs. The calculation requires a taxpayer to: (a) identify MP and MPC types; (b) track relevant characteristics of each MP and MPC; (c) determine direct costs; and (d) determine PFE direct costs. A separate Clean Electricity MACR must be calculated for each qualified facility or EST placed in service during a taxable year.

Eligible Component MACR

For Section 45X eligible components, the Eligible Component MACR substitutes "total direct material costs" for "total direct costs," focusing on the constituent elements, materials, or subcomponents ("Constituent Materials") incorporated into or consumed in the production of the eligible component. The relevant costs are those paid or incurred by the taxpayer for direct materials under Section 1.263A-1(e)(2)(i)(A), including freight-in and tariffs.

Interim Safe Harbors: The Core of the Notice

The most consequential aspect of Notice 2026-15 is its three-tiered interim safe harbor framework, which is intended to significantly simplify the compliance burden.

Identification Safe Harbor

The Identification Safe Harbor allows taxpayers to use the 2023–2025 domestic content safe harbor tables (from Notices 2023-38, 2024-41, and 2025-08) as the exclusive and exhaustive list of MPs and MPCs (or Constituent Materials) for purposes of identifying what must be tracked and costed. Components not appearing in the tables are disregarded entirely and do not factor into the MACR calculation. This is material compliance relief, it obviates the need for deeper upstream tracing that many in the industry feared and instead limits the inquiry to a discrete, published list of components.

However, this pathway is available only for projects and components listed in the safe harbor tables. Facility types without specified tables, such as nuclear, fuel cells, or geothermal, cannot use this safe harbor. Likewise, facilities relying on the incremental production rule cannot use the Cost Percentage Safe Harbor. The Treasury has acknowledged these industries' interest in obtaining updated tables, but guidance remains forthcoming.

Cost Percentage Safe Harbor

Building on the Identification Safe Harbor, the Cost Percentage Safe Harbor permits taxpayers to use the Assigned Cost Percentages from the safe harbor tables in lieu of tracking actual direct costs. The taxpayer sums the Assigned Cost Percentages for each listed MP and MPC (the "Total Percentage"), sums the Assigned Cost Percentages attributable to PFE-produced MPs and MPCs (the "Total PFE Percentage"), and calculates the MACR as: $(\text{Total Percentage} - \text{Total PFE Percentage}) / \text{Total Percentage}$.

Structural steel and iron are excluded entirely from the MACR calculation, consistent with their treatment under the domestic content rules. Used property in facilities qualifying under the 80/20 rule is also disregarded; only the costs of new MPs and MPCs count toward the calculation. The Notice's examples, particularly the PV facility illustration walking through both safe harbors, will be invaluable in standardizing the calculation methodology.

Certification Safe Harbor

The Certification Safe Harbor provides an alternative pathway allowing taxpayers to rely on supplier certifications to determine direct costs, PFE direct costs, and PFE status. Three certification forms are available, tracking the statutory framework in Section 7701(a)(52)(D)(iii)(II)(bb): (AA) an attestation that the property was not produced or manufactured by a PFE and the supplier has no knowledge of PFE involvement in the upstream chain; (BB) for Section 45X, a statement of total direct material costs not produced or manufactured by a PFE; or (CC) for Sections 45Y/48E, a statement of total direct costs attributable to

non-PFE manufactured products. Importantly, pathways (BB) and (CC) do not facially require the supplier to possess knowledge of the entire upstream chain, as does pathway (AA).

Certifications must include the supplier's employer identification number (or foreign equivalent), be signed under penalties of perjury, be retained for at least six years by both the supplier and the taxpayer, and be produced upon IRS request. A taxpayer may rely on a certification unless it "knows or has reason to know" the certification is inaccurate. The "reason to know" standard is the most significant area of ambiguity in the Notice and is driving intense market discussions. Early practice suggests a tiered diligence approach: baseline certifications with PFE-status checklists from established suppliers, supplemented for higher-risk Tier 2 suppliers and battery storage components by third party supply chain audits. Suppliers offering compliance packages, including legal memoranda and compliance presentations, are gaining a competitive edge.

Tracking and Averaging Flexibility

The Notice provides meaningful flexibility in how taxpayers track components to specific facilities or eligible components. Three tracking methods are available:

- **Individual tracking.** The default approach requiring each MP or MPC to be traced to the specific facility or EST into which it is incorporated.
- **De minimis assignment-based tracking.** Allows MPs or MPCs of the same type to be assigned across qualified facilities or ESTs placed in service during the same taxable year without individual tracing, provided the assigned components represent less than 10% of the Total Direct Costs of each facility.
- **Average-cost tracking for small ESTs.** For ESTs of the same type, each under 1 MW, placed in service during the same taxable year, taxpayers may use averaged costs and PFE Production Percentages over specified periods within the taxable year.

Section 45X manufacturers may use a similar averaging system for Constituent Materials incorporated into eligible components during specified time periods.

Binding Written Contract Election

A notable feature of the statutory framework, addressed in the Notice, is the elective grandfather provision under Section 7701(a)(52)(D)(iv). Upon a taxpayer's election, MPs, eligible components, or Constituent Materials acquired or manufactured pursuant to a binding written contract entered into before June 16, 2025, and placed in service before January 1, 2030 (or January 1, 2028 for applicable wind facilities) in a facility where construction began before August 1, 2025, may be excluded from the MACR calculation entirely. For Constituent Materials, the item must be used in a product sold before January 1, 2030 (or January 1, 2027 for Section 45X). Treasury has been granted anti-abuse authority to prevent stockpiling of components during any period prior to the application of the PFE requirements.

Qualified Interconnection Property

The Notice addresses the separate treatment of qualified interconnection property under Section 48E with a nuanced approach. A taxpayer seeking to include interconnection property expenditures in its qualified investment must calculate a separate Clean Electricity MACR for the interconnection property, apart from the facility itself. Each project component: solar, storage, and interconnection, qualify independently; failure on one does not disqualify the others. However, the safe harbors are unavailable for interconnection property, requiring the direct cost method, with practitioners view as significantly more invasive and more susceptible to error.

Effective Control and Anti-Abuse Provisions

Notice 2026-15 previews forthcoming regulatory action on two important fronts. First, the Notice clarifies that effective control under the foreign-influenced entity provisions of Section 7701(a)(51)(D) is determined independently under each prong of the statute. Notably, any licensing agreement for intellectual property with respect to a qualified facility entered into or modified on or after July 4, 2025, constitutes effective control, even absent any of the other enumerated prohibited provisions, such as

limits on IP usage.

Second, Treasury and the IRS intend to propose regulations to prevent entities from evading, circumventing, or abusing the PFE restrictions, including through temporary lapses of restricted foreign ownership or control.

Suppliers restructuring ownership of supply chains mid-stream to achieve compliance raise particularly difficult questions, as the rule lack specificity on the timing of qualification relative to procurement and delivery.

Enhanced Penalty and Statute of Limitations Framework

The OBBBA established a robust penalty regime supporting the PFE rules. New Section 6662(m) lowers the substantial understatement threshold to 1% (from 10%) for credit disallowances attributable to overstating the MACR. New Section 6501(o) extends the statute of limitations to six years for deficiencies attributable to MACR determination errors. New Section 6695B imposes a separate penalty on suppliers who provide certifications they know or should have known to be inaccurate, equal to the greater of 10% of the resulting underpayment or \$5,000, though a reasonable cause defense is available.

Reliance and What Comes Next

Taxpayers may rely on the guidance in Sections 3 and 5.01 of the Notice for projects that begin construction after December 31, 2025, and continue through 60 days after publication of the forthcoming proposed regulations. The Section 4 safe harbors may be relied upon through 60 days after publication of the forthcoming safe harbor tables under Section 7701(a)(52)(D)(iii)(I), which must be issued by December 31, 2026.

While Notice 2026-15 resolves several of the most pressing compliance questions confronting the clean energy tax credit market, particularly around supply-chain depth, cost allocation methodology, and certification standards, it expressly defers comprehensive guidance on the PFE definitional framework, constructive ownership mechanics, and long-term recapture rules to forthcoming proposed regulations. Stakeholders should use the comment period strategically and begin integrating the safe harbor frameworks into project and deal structures without delay.

The early market consensus is that Notice 2026-15, while demanding increased diligence and documentation relative to the domestic content regime, provides workable and solvable rules. Storage remains the highest-risk area given the battery supply chain's continued dependence on Chinese components. Stakeholders should engage counterparties and advisors early, integrate the safe harbor frameworks into deal structures without delay, and prepare for escalating MACR thresholds in future years.