



TaxNewsFlash

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Notice 2021-35: Carbon oxide sequestration credit, inflation adjustment factor for 2021 under section 45Q

Notice 2021-35 provides the inflation adjustment factor for the credit for carbon oxide sequestration under section 45Q for calendar year 2021. The inflation adjustment factor is used to determine the amount of the credit allowable under section 45Q.

Notice 2021-35—which appears in Internal Revenue Bulletin 2021-46 (dated Monday, November 15, 2021)—also provides that the IRS, in consultation with the Environmental Protection Agency (EPA), does not certify that the aggregate amount of qualified carbon oxide taken into account for purposes of section 45Q has reached 75 million metric tons. This is based on information available to the IRS and EPA as of October 26, 2021.

Read Notice 2021-35 in [IRB-2021-46](#) [PDF 648 KB]

Background

Prior to the enactment of the Bipartisan Budget Act of 2018 (“BBA”), the section 45Q credit for carbon oxide sequestration provided a tax credit for qualified carbon dioxide captured by the taxpayer at a qualified facility and disposed of in secure geological storage or used as a tertiary injectant in an enhanced oil or gas recovery (EOR) project. The credit was capped at a total of 75 million metric tons of qualified carbon oxide captured by all taxpayers.

Notice 2021-35 provides that, for 2021, the credit rates for qualified carbon oxide captured by the taxpayer using carbon capture equipment originally placed in service prior to February 9, 2018 (the date of enactment of the BBA) are \$24.10 per metric ton for qualified carbon oxide disposed of in secure geological storage, and \$12.05 per metric ton for qualified carbon oxide used by the taxpayer as a tertiary injectant in an EOR project or utilized by the taxpayer.

With the enactment of the BBA, the section 45Q credit for carbon capture equipment was significantly expanded to include higher credit rates and no cap, among other favorable changes, for carbon capture equipment placed in service on or after February 9, 2018.

KPMG observation

Many tax professionals expected that the 75 million metric ton cap would be reached this year, so the news provided by Notice 2021-35 is surprising. Last year, in Notice 2020-40, the IRS stated that 72,087,903 metric tons of qualified carbon oxide had been taken into account, which was an increase of over 9.3 million metric tons from 2019.

It is interesting that the IRS typically publishes this inflationary notice in the spring/summer, but this year waited until November to publish the notice. Some believe this likely means that the IRS is very close to certifying that the cap has been met, and it will likely be met in 2022, if not in the last few months of 2021.

Going forward, taxpayers may want to consider upgrading their equipment so that it is treated as newly placed in service, and therefore eligible to claim section 45Q credits. This is especially true because post-BBA section 45Q offers higher credits rates and, in addition, recent legislative proposals indicate that the section 45Q credit may become refundable.

The Treasury regulations permit carbon capture equipment to qualify as originally placed in service, even if it contains some used components of property, as long as the fair market value of the used components is not more than 20% of the qualified facility or carbon capture equipment's total value ("80/20 Rule").

Inflation adjustment factor

Notice 2021-35 provides:

- The inflation adjustment factor for calendar year 2021 is 1.2049.
- The section 45Q credit for calendar year 2021 is:
 - \$24.10 per metric ton of qualified carbon oxide under section 45Q(a)(1).
 - \$12.05 per metric ton of qualified carbon oxide under section 45Q(a)(2).

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