



KPMG report: Initial observations on guidance relating to clean vehicle credit under section 30D

January 5, 2023



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Introduction

The IRS and the Treasury Department recently released three items of guidance addressing the amendments to the new clean vehicle credit under section 30D, as amended by Pub. L. No. 117-169 (commonly called the “Inflation Reduction Act” or the “**IRA**”):

- [Notice 2023-1](#) [PDF 118 KB] addressing the expected definitions in forthcoming proposed regulations for certain defined terms in section 30D (the “**notice**”);
- A [whitepaper](#) [PDF 432 KB] discussing what guidance on the critical minerals and battery component requirements will be released (the “**whitepaper**”); and
- A [fact sheet](#) [PDF 387 KB] containing a frequently asked questions list includes 27 questions and answers relating to the current application of the new clean vehicle credit (the “**FAQ list**”).

In this article each of these guidance items are addressed in turn.

Notice 2023-1

Section 30D provides a credit of up to \$7,500 in connection with the purchase of a qualified clean vehicle. In addition to other changes the IRA added five requirements for a taxpayer to be eligible for the section 30D credit:

- Final assembly of the vehicle must have taken place in North America (the “**Final Assembly Requirement**”);
- A rising percentage of critical minerals used in the clean vehicle’s battery must be extracted or processed by the U.S. or any country with which the U.S. has a free trade agreement in effect (the “**Critical Minerals Requirement**”);
- A rising percentage of battery components must be manufactured or assembled in North America (the “**Battery Component Requirement**”);
- Taxpayers are only eligible for the credit if their modified adjusted gross income (**MAGI**) is below certain thresholds, depending on the type of taxpayer (the “**MAGI Limitation**”); and
- Clean vehicles, depending on the type, are only eligible for the credit to the extent the manufacturer’s suggested retail price (“**MSRP**”) of the clean vehicle is below a cap (the “**MSRP Limitation**”).

When the Critical Mineral Requirement and Battery Component Requirement become applicable, the credit amount is tied to meeting the requirements. Specifically, a vehicle satisfying both the Critical Mineral Requirement (\$3,750) and the Battery Component Requirement (\$3,750) is how the maximum \$7500 per vehicle credit can be achieved.

The notice announces that Treasury and IRS intend to issue proposed regulations under section 30D. The notice also provides some relatively straightforward definitional guidance relating to the Final Assembly Requirement, the MAGI Limitation, and the MSRP Limitation. The notice does not, however, include guidance relating to the Critical Mineral Requirement or the Battery Component Requirement. Please see the discussion below of the whitepaper for insights as to what type of guidance and definitions may be issued for the Critical Minerals and Battery Component Requirements.

As to the Final Assembly Requirement, the notice defines two terms: “Final Assembly” and “North America.” Final Assembly is defined as:

the process by which a manufacturer produces a new clean vehicle at, or through the use of, a plant, factory, or other place from which the vehicle is delivered to a dealer or importer with all component parts necessary for the mechanical operation of the vehicle included with the vehicle, whether or not the component parts are permanently installed in or on the vehicle.

The notice provides two methods a taxpayer can rely on to establish the location of final assembly: (1) the vehicle's plant of manufacture as reported in the vehicle identification number pursuant to 49 CFR 565; or (2) the final assembly point reported on the label affixed to the vehicle as described in 49 CFR 583.5(a)(3).

North America is defined as the territory of the U.S, Canada, and Mexico as defined in 19 CFR part 182, Appendix A, § 1(1).

As to the MSRP Limitation, MSRP is defined as the sum of: (1) the retail price of the automobile suggested by the manufacturer as described in 15 USC 1232(f)(1); and (2) the retail delivered price suggested by the manufacturer for accessories or items of optional equipment physically attached to such automobile at the time of its delivery to the dealer which is not included in the amount determined in (1).

KPMG observation

The MSRP Limitation does not appear to pick up the cost of any aftermarket items a taxpayer may purchase for a clean vehicle. This includes so-called over-the-air upgrades ("OTAs") such as unlocking additional battery capacity or adding self-driving features. A manufacturer may be incentivized not to include OTAs in the MSRP to meet the cap.

For the MSRP Limitation, the notice points taxpayers to the rules and definitions provided in 40 CFR 600.002 for vans, sport utility vehicles, and pickup trucks (all with a MSRP cap of \$80,000). Other vehicles, as described in section 30D(f)(11)(B)(iv), are vehicles that are not considered a van, sport utility vehicle, or pickup truck (all with a MSRP cap of \$55,000).

Whitepaper

The whitepaper discusses the "anticipated direction" of to-be-released proposed regulations covering the Critical Minerals and Battery Component Requirements. As discussed [below] in the FAQ list overview, proposed guidance must be issued by the IRS and Treasury prior to the Critical Minerals and Battery Component Requirements becoming effective, and it is expected that such guidance will be released in March 2023. Once proposed guidance is issued, vehicle manufacturers will be required to certify whether their vehicles meet the Critical Mineral and Battery Component Requirements.

Highlighting the "importance of continued communication with stakeholders," the stated purpose of the whitepaper is to "promote transparency ahead of the issuance of proposed guidance currently being developed." Somewhat in contrast with a taxpayer's ability to rely on the FAQ list for certain penalty relief, the whitepaper caveats that the discussion therein does not "create any right or benefit, substantive or procedural, enforceable at law or in equity by any party."

Critical Minerals Requirement

With respect to the Critical Minerals Requirement, the whitepaper recites the statutory requirements, generally that a rising percentage of critical minerals used in a clean vehicle's battery must be extracted or processed by the U.S. or any country with which the U.S. has a free trade agreement in effect for the clean vehicle to be credit-eligible. The whitepaper goes on to define the following terms: (1) extraction; (2) processing; (3) recycling; (4) constituent materials; (5) value; (6) value added; and (7) free trade agreement; each for purposes of the Critical Minerals Requirement.

Further, the whitepaper acknowledges the difficulty for manufacturers to track their battery supply chains, and in response the whitepaper lays out a three-step process that is intended to apply as a transition rule for 2023 and

2024. Effectively, this transition rule would provide relief by way of a “value added” test—so long as 50% or more of the value added of the critical mineral extraction, or processing, occurs in the United States or in any country with which the United States has a free trade agreement in effect, then 100% of the critical mineral will be treated as a “qualifying critical mineral.” A similar 50% value add threshold would apply for the recycling of critical minerals and determining whether such recycling took place in North America. In short, a “mixed-source” critical mineral will count as a qualifying critical mineral, in 2023 and 2024, so long as at least 50% of the “value add” takes place in (1) the United States or in any country with which the United States has a free trade agreement in effect (for extraction and processing) or (2) North America (for recycling).

Finally, as to the Critical Minerals Requirement, the whitepaper discusses proposed flexibility for taxpayers in determining (1) the date on which to value the critical minerals and (2) the averaging methodology used with respect to vehicles from the same model line, plant, class, or some combination thereof, with final assembly in North America.

Battery Component Requirement

For the Battery Component Requirement, the whitepaper recites the statutory requirement that a rising percentage of battery components must be manufactured or assembled in North America. The whitepaper goes on to define the following terms: (1) battery cell; (2) battery component; (3) constituent materials; (4) manufacturing; (5) assembly; (6) value; and (7) incremental value; each for purposes of the Battery Component Requirement.

The whitepaper then sets forth a proposed four-step process that could be used for purposes of determining the percentage of the value of battery components that goes toward meeting the Battery Component Requirement. The whitepaper goes on to discuss proposed flexibility for taxpayers, similar to that described above for the Critical Minerals requirement, in determining (1) the date on which to value the battery components and (2) the averaging methodology used with respect to vehicles from the same model line, plant, class, or some combination thereof, with final assembly in North America.

KPMG observation

The whitepaper provides some helpful information regarding the expected application of the Critical Mineral Requirement and the Battery Component Requirement. For instance, the whitepaper provides some useful clarifying information such as stating that “critical minerals” for purposes of section 30D refers to the applicable critical minerals defined in the Section 45X (the advanced manufacturing production tax credit) and identifying what items are included as battery components.

In addition, the whitepaper indicates some effort to offer flexibility by providing, for example, the 50% value add determination for critical minerals in 2023 and 2024 and the availability of averaging methodologies. Although even with that flexibility the tracking of materials and supply chains is likely to be a challenge for many stakeholders.

FAQ list

In addition to the notice and the whitepaper, the IRS and Treasury also released a list of frequently asked questions relating to the implementation of the new section 30D rules as well as addressing certain questions on the transition process to the new section 30D regime.¹ Although the FAQ list is not official guidance, the IRS

¹ The FAQ list also addresses questions related to the credit for previously-owned clean vehicles under section 25E and the credit for qualified commercial clean vehicles under section 45W.

does provide mitigation of penalties that offer reasonable cause relief for taxpayers who “reasonably and in good faith” rely on the FAQ list.²

The IRS indicated that the FAQ list is a live document, meaning it will be continuously updated on the IRS website. Note that the IRS does maintain an archive of prior FAQs as they are superseded.

The FAQ list includes both questions that are already answered in the statute as well as interpretive questions relating to the application of the new section 30D rules and the transition from the pre-IRA code provision. Of note, some of the prior section 30D rules still apply and some of the new section 30D rules do not yet apply, including the Critical Minerals and Battery Component Requirements, as the IRS has not yet issued the necessary statutory guidance for those two requirements to become active.

Some of the more interesting answers are highlighted in the following list:

- The IRS plans to maintain a [list of eligible vehicles](#)—it remains the taxpayer’s responsibility to confirm that the Final Assembly Requirement and the MSRP Limitation are met, even if a vehicle appears on this list;
- The credit is claimed by an individual upon delivery of the new clean vehicle, even if the taxpayer ordered it in a prior year;
- The credit amount is calculated under the prior section 30D formula until proposed guidance is issued addressing the Critical Mineral and Battery Component requirements (i.e., neither of these requirements is yet applicable, proposed guidance is expected to be issued in March 2023);
- The clean vehicle credit may not be refunded or carried forward;
- Taxpayers must include the VIN of a credit-eligible new clean vehicle on Form 8936, *Qualified Plug-In Electric Drive Motor Vehicle Credit*;
- The eventual total purchase price paid by a taxpayer is not relevant for determining credit eligibility under the MSRP Limitation; only the MSRP itself is relevant; and
- For vehicles sold in 2022 and delivered in 2023, the sales cap of 200,000 vehicles per manufacturer continues to apply as the new clean vehicle was sold in 2022. Further, the MSRP and MAGI Limitations also would apply due to delivery taking place in 2023.

The FAQ list also includes some answers of interest to the section 45W commercial clean vehicle credit, in particular relating to credit eligibility of lessors of vehicles:

- If a taxpayer leases clean vehicles to its customers the taxpayer can claim the section 45W credit, provided the lease is respected as a lease for tax purposes. Features of a vehicle lease agreement that would make it more likely to be recharacterized as a sale include, but are not limited to:
 - A lease term that covers more than 80% to 90% of the economic useful life of the vehicle
 - A bargain purchase option at the end of the lease term (that is, the ability to purchase the vehicle at less than its fair market value at the end of the term) or other terms/provisions in the lease that economically compel the lessee to acquire the vehicle at the end of the lease term

² Specifically, this is what the Fact Sheet provides regarding a taxpayer’s ability to rely on its contents:

Because these FAQs have not been published in the Internal Revenue Bulletin, they will not be relied on or used by the IRS to resolve a case. Similarly, if an FAQ turns out to be an inaccurate statement of the law as applied to a particular taxpayer’s case, the law will control the taxpayer’s tax liability. Nonetheless, a taxpayer who reasonably and in good faith relies on these FAQs will not be subject to a penalty that provides a reasonable cause standard for relief, including a negligence penalty or other accuracy-related penalty, to the extent that reliance results in an underpayment of tax.

- Lease terms that result in the lessor transferring ownership risk to the lessee, for example, a terminal rental adjustment clause (TRAC) provision that requires the lessee to pay the difference between the actual and expected value of the vehicle at the end of the lease.

KPMG observation

While the statutory language of section 45W appears to clearly allow a lessor of clean vehicles to claim the section 45W credit, the confirmation of this point provided by the FAQ list is helpful.

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