Tax Notes

The New Commercial Clean Vehicle Credit

By Michael J. Andriola, CPA, Partner and Elisha M. Brestovansky, CPA, MBA, Senior Tax Manager

The Plug-In Electric Vehicle Tax Credit under Internal Revenue Code (IRC) Sec. 30D was originally enacted with the Energy Improvement and Extension Act of 2008 and has been extended multiple times since its enactment. The President signed the Inflation Reduction Act of 2022 (the Act) on August 17, 2022 which includes changes to the Plug-in Electric Vehicle Tax Credit (now known as the Clean Vehicle Credit) that will impact both individuals and businesses. (See our FAQs article here on the individual credit.)

Under the original codification, qualifying vehicles purchased for either personal or business use were eligible for a tax credit between $2,000 and $7,500 depending on the battery's level of energy output. The credit phased out beginning with the second calendar quarter following the calendar quarter in which vehicles manufactured by the manufacturer exceeded 200,000 units. The Act created a new IRC Sec. 45W to cover the **business portion** of the Clean Vehicle Credit effective for qualifying vehicles placed in service after December 31, 2022. The changes in the rules for the credit may be a boon to businesses. Read on for more details about the new version of the credit.

Eligibility

The vehicle must be a qualified commercial clean vehicle. The vehicle must meet the following requirements:

1. The vehicle must be acquired for use or lease by the business;
2. The vehicle must be a depreciable asset;
3. The vehicle must be manufactured for use on streets, roads and highways or must be mobile machinery;
4. The vehicle's battery capacity must be at least 7 kWh (15 kWh for vehicles weighing more than 14,000 pounds);
5. The vehicle must be charged by an external electricity source; and
6. The vehicle must made by a *qualified* manufacturer.

Notably, the Act removes the limit on the credit for manufacturers that have exceeded 200,000 units. This opens up the credit significantly, as major manufacturers had previously hit that cap.

Amount of the Credit

The amount of the credit will be the lesser of:

1. 15% of the vehicle's cost (30% for vehicles not powered by a gas or diesel engine); ***or***
2. The "incremental cost" of the vehicle over the cost of a comparable vehicle powered solely by a gas or diesel engine.

The credit will be capped at a maximum credit of $7,500 for vehicles with a gross vehicle weight rating (GVWR) of less than 14,000 pounds or $40,000 for vehicles over 14,000 pounds.

Other Restrictions

Like the Clean Vehicle Credit for individuals, the IRS will be tracking the credits by Vehicle Identification Number (VIN). Taxpayers claiming the credit will be required to provide the VIN on the tax form used to claim the credit. There is one credit available per VIN.

In addition, once the credit has been claimed, the cost basis of the vehicle must be reduced by the amount of the credit before depreciation is taken. There is no double benefit permitted.
Lastly, the vehicle must be used in the United States to be eligible for the credit.

Observations

The limits on the Commercial Clean Vehicle Credit under IRC Sec. 45W are much less stringent than the Clean Vehicle Credit for individuals under IRC Sec. 30D.

As discussed in our prior article, the credit for individuals has key requirements that could make it difficult to access. Taxpayers utilizing the commercial credit are not subject to the Modified Adjusted Gross Income (MAGI) limitations, vehicle MSRP pricing caps, the mineral and battery component requirements and the final assembly requirements as imposed under IRC 30D for individuals.
IRS guidance is still needed to determine the incremental cost threshold portion of the credit limitation; however, it appears that the credit will be much easier for taxpayers to claim at the business level. In addition, taxpayers will be able to claim a much larger credit ($40,000) for qualifying vehicles over 14,000 pounds, such as the Tesla Electric Semi-truck with an MSRP upwards of $150,000.

Practical Considerations

When considering if investing in electric vehicles may be a viable business strategy, there are numerous things to consider, like the cost of insurance. Since the vehicle must be owned by the business, the insurance would have to be provided for the business use of the vehicle, which is typically more costly than insurance for personal use.

Another consideration is the vast improvement in technology. Batteries are being engineered to perform more efficiently at a rapid pace, but the cost of battery replacement on an electric vehicle may be many thousands of dollars if not covered under a warranty. Warranties typically cover electric vehicle batteries for a minimum of eight years or up to 100,000 miles. Before making a significant investment in technology, one should consider the useful life and repairs costs of the technology in which they are investing.

Taxpayers must also consider whether there will be a secondary market for these vehicles. One business strategy is to purchase a new vehicle which will be kept in use for the entirety of its depreciable life and then once fully depreciated, sell the vehicle at auction to help fund its replacement. If the potential subsequent buyer of the vehicle is not entitled to the commercial Clean Vehicle Credit because you're limited to one credit per VIN and the technology of the battery could be relatively obsolete after the vehicle's depreciable life is exhausted, would there realistically be a secondary market in which to sell? Weighing and balancing the amount of the tax credit versus the premium you will be paying for the use of new technology will be an important business decision for you to make. While the environmental considerations are also extremely important, a business owner must decide if they can afford to make the investment.

On the other hand, businesses should also consider state legislation that mandates zero-emissions. New York passed a bill in 2021 that mandates zero-emissions on all passenger cars and trucks sold or leased in New York by 2035. California also has a similar policy and more states are following suit. As more and more states pass zero-emission legislation, electric vehicles will become more commonly used and businesses may miss opportunities to take advantage of federal and state incentives.

Contact Us

If you have any questions about the commercial Clean Vehicle Credit, contact your client service partner or:

Michael J. Andriola, CPA
Partner
mandriola@pkfod.com | 908-967-6815

Elisha M. Brestovansky, CPA, MBA
Senior Tax Manager
ebrestovansky@pkfod.com | 845-670-7140