

January 2024

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Treasury Issues Proposed Regulations on the Section 30D Clean Vehicle Tax Credit's Foreign Entity of Concern Rules

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The Inflation Reduction Act of 2022 brought about modifications to the clean vehicle tax credit available under Section 30D of the U.S. Internal Revenue Code of 1986, as amended (the "Code" and such credit, the "Clean Vehicle Tax Credit"). Code Section 30D allows taxpayers to claim the Clean Vehicle Tax Credit for each new clean vehicle placed in service during the taxable year. However, certain limitations exist, notably under the Excluded Entities Rule, which restricts the credit for vehicles meeting specific criteria. According to the Excluded Entities Rule, the Clean Vehicle Tax Credit is not allowed for (i) any vehicle placed in service after December 31, 2024, if any of the "applicable critical minerals" contained in the battery of that vehicle were "extracted, processed, or recycled" by a "foreign entity of concern" ("FEOC") as defined in Section 40207(a)(5) of the Infrastructure Investment and Jobs Act (the "IIJA") or (ii) any vehicle placed in service after December 31, 2023, if any of the components contained in the battery of that vehicle were "manufactured or assembled" by an FEOC (together, the "Excluded Entities Rule").

On December 1, 2023, the Department of the Treasury issued [proposed regulations](#) (the "Proposed Regulations") that would provide clarity regarding the Excluded Entities Rule. Concurrently, the Department of Energy (the "DoE") released [proposed guidance](#) that would provide proposed interpretations of certain terms used to define an FEOC.

Foreign Entity of Concern

The IIJA defines an FEOC to include foreign entities "owned by, controlled by, or subject to the jurisdiction or direction of a government" of a covered nation (*i.e.*, China, Russia, North Korea and Iran).¹ In its guidance, the DoE provided the following interpretations of terms applicable to the FEOC determination:

- "foreign entity" means any of the following:
 - a. a government of a foreign country;
 - b. a natural person who is not a lawful permanent resident, citizen or any other protected individual of the United States;
 - c. a partnership, association, corporation, organization or other combination of persons organized under the laws of or having its principal place of business in a foreign country; or

- d. an entity organized under the laws of the United States that is “owned by, controlled by, or subject to the direction” of an entity that qualifies as a foreign entity in any of the above clauses.
- **“government of a foreign country”** means any of the following:
 - a. a national or subnational government of a foreign country;
 - b. an agency or instrumentality of a national or subnational government of a foreign country;
 - c. a dominant or ruling political party (e.g., Chinese Communist Party) of a foreign country;
or
 - d. a current or former senior foreign political figure.
- A foreign entity is **“subject to the jurisdiction”** of a covered nation government if:
 - a. the foreign entity is incorporated or domiciled in, or has its principal place of business in, a covered nation; or
 - b. with respect to the critical minerals, components, or materials of a given battery, the foreign entity engages in the extraction, processing, or recycling of such critical minerals, the manufacturing or assembly of such components, or the processing of such materials, in a covered nation.
- An entity is **“owned by, controlled by, or subject to the direction”** of another entity (including the government of a foreign country that is a covered nation) if:
 - a. 25% or more of the entity’s board seats, voting rights, or equity interests are cumulatively held by that other entity, whether directly or indirectly via one or more intermediate entities;
or
 - b. with respect to the critical minerals, battery components, or battery materials of a given battery, the entity has entered into a licensing arrangement or other contract with a contractor that entitles that contractor to exercise effective control over the extraction, processing, recycling, manufacturing, or assembly of the critical minerals, battery components, or battery materials that would be attributed to the entity.

For purposes of determining control by a foreign entity (including the government of a foreign country), control is evaluated based on the combined interest in an entity held, directly or indirectly, by all other entities that qualify under the above interpretation of “foreign entity.” For purposes of determining whether an entity indirectly holds board seats, voting rights, or equity interest, if a parent (including the government of a foreign country) directly holds 50% or more of a subsidiary’s board seats, voting rights, or equity interest, then any holdings of the subsidiary are fully attributed to the parent. However, if a parent directly holds less than 50% of a subsidiary’s board seats, voting rights, or equity interest, then indirect ownership is attributed proportionately.

FEOC-Compliance Requirements

Under the Proposed Regulations, a battery is FEOC-compliant if the battery components and applicable critical minerals of such battery are FEOC-compliant.

For new clean vehicles placed in service after December 31, 2023, the Proposed Regulations would provide that the determination of whether a battery is FEOC-compliant follows the following process:

1. The qualified manufacturer determines whether battery components and applicable critical minerals (and associated constituent materials) are FEOC-compliant;
2. The FEOC-compliant battery components and FEOC-compliant applicable critical minerals (and associated constituent materials) are physically tracked to specific battery cells² (unless such materials are allocated to battery cells without physical tracking and instead the determination is based on an allocation of available mass, produced or contracted for, of applicable critical minerals and their associated constituent materials); and
3. The battery components, including battery cells, are physically tracked to specific batteries.

The Proposed Regulations would thus impose the following requirements with respect to the battery components and minerals included in a new clean vehicle:

Component	Applicable to new clean vehicles placed in service:	FEOC Requirement	Tracking Requirement
Battery Component (other than a battery cell)	After 12/31/2023	Not manufactured or assembled by an FEOC	FEOC-compliant battery components of a battery, including battery cells, must be physically tracked to such battery.
Applicable critical mineral	After 12/31/2024	Not extracted, processed, or recycled by an FEOC	
Battery cell	After 12/31/2023 and before 1/1/2025	(i) Not manufactured or assembled by an FEOC; and (ii) Contains only FEOC-compliant battery components	FEOC-compliant battery components must be physically tracked to specific battery cells and the mass of FEOC-compliant applicable critical minerals and associated constituent materials must be physically tracked to specific battery cells; alternatively, only for any new clean vehicle for which the qualified manufacturer provides a periodic written report before January 1, 2027, the determination that a battery cell is an FEOC-compliant battery cell may be based on an allocation of available mass, produced or contracted for, of applicable critical minerals and their associated constituent materials to
	After 12/31/2024	(i) Not manufactured or assembled by an FEOC; and (ii) Contains only FEOC-compliant battery components and FEOC-compliant	

Component	Applicable to new clean vehicles placed in service:	FEOC Requirement	Tracking Requirement
		applicable critical minerals	specific battery cells manufactured or assembled in a battery cell production facility, without the physical tracking
Battery	After 12/31/2023	Contains only FEOC-compliant battery components (other than battery cells) and FEOC compliant battery cells (as described above)	

Definitions

The Proposed Regulations would apply the following definitions with respect to the first prong of the Excluded Entities Rule that for any vehicle placed in service after December 31, 2024, no “applicable critical minerals” contained in the battery of that vehicle may have been “extracted, processed, or recycled” by an FEOC:

- **“Applicable critical mineral”** means an applicable critical mineral as defined in Code Section 45X(c)(6). In other words, it would use the same definition as an “applicable critical mineral” for purposes of the advanced manufacturing production credit.
- **“Extraction”** means the activities performed to harvest minerals or natural resources from the ground or a body of water. Extraction concludes when activities are performed to convert raw mined or harvested products or raw well effluent to substances that can be readily transported or stored for direct use in critical mineral processing. Extraction includes the physical processes involved in refining but does not include the chemical and thermal processes involved in refining.
- **“Processing”** means the non-physical processes involved in the refining of non-recycled substances or materials, including the treating, baking, and coating processes used to convert such substances and materials into constituent materials. Processing includes the chemical or thermal processes involved in refining and does not include the physical processes involved in refining.
- **“Recycling”** means the series of activities during which recyclable materials containing critical minerals are transformed into specification-grade commodities and consumed in lieu of virgin materials to create new constituent materials.

The Proposed Regulations would also apply the following definitions with respect to the second prong of the Excluded Entities Rule that for any vehicle placed in service after December 31, 2023, none of the “battery components” contained in the battery of that vehicle may have been “manufactured or assembled” by an FEOC:

- **“Battery component”** means a component that forms part of a battery and that is manufactured or assembled from one or more components or constituent materials that are combined through industrial, chemical, and physical assembly steps. Battery components may include, but are not limited to, a cathode electrode, anode electrode, solid metal electrode, separator, liquid electrolyte, solid state electrolyte, battery cell, and battery module.
- **“Constituent materials”** means materials that contain applicable critical minerals and that are employed directly in the manufacturing of battery components. Constituent materials may include, but are not limited to, powders of cathode active materials, powders of anode active materials, foils, metals for solid electrodes, binders, electrolyte salts, and electrolyte additives, as required for a battery cell.
- **“Manufacturing”** means the industrial and chemical steps taken to produce a battery component.
- **“Assembly”** means the process of combining battery components into battery cells and battery modules.

Compliance Review and Due Diligence

The Proposed Regulations would require that a qualified manufacturer provide attestations, certifications and documentation demonstrating compliance with the requirements of Code Section 30D(e) for any new clean vehicle placed in service after December 31, 2024.

A qualified manufacturer of a new clean vehicle would also be required to conduct due diligence on all relevant battery components and applicable critical minerals (and associated constituent materials) contained in any new clean vehicle to determine whether those components or minerals are FEOC-compliant. In this diligence process, the qualified manufacturer must comply with standards of tracing for battery materials available in the industry at the time of the attestation or certification, and it may reasonably rely on a supplier attestation or certification unless it knows or has reason to know after conducting diligence that the supplier attestation or certification is incorrect. The IRS will not consider a battery to be FEOC-compliant unless the qualified manufacturer has conducted this due diligence and provided required attestations or certifications.

The Proposed Regulations would also incorporate a transition rule that would temporarily exclude a specific list of identified non-traceable battery materials from the due diligence requirements of the qualified manufacturers. Under this transition rule, with respect to any new clean vehicles for which a qualified manufacturer provides a periodic written report before January 1, 2027, the qualified manufacturer may satisfy its due-diligence requirement by excluding specified non-traceable battery materials (and associated constituent materials). In addition, the qualified manufacturer may exclude those materials from the determination of whether a battery cell is FEOC-compliant. To rely on this rule, the qualified manufacturer must submit a report demonstrating how the qualified manufacturer will comply with the Excluded Entities Rule once the rule is no longer in effect.

In addition to the diligence process described above, the Proposed Regulations would require that for new clean vehicles placed in service after December 31, 2024, a qualified manufacturer must determine and provide information to the IRS to establish a compliant-battery ledger for each calendar year.

The Proposed Regulations would grant the IRS the authority to take certain actions against a qualified manufacturer if it determines that a qualified manufacturer has provided inaccurate attestations, certifications and documentation.

Next Steps: Comment Period, Public Hearing, and Future Guidance

Interested parties may submit written comments on the Proposed Regulations through January 18, 2024. The Proposed Regulations also invite public comments on traceability issues of certain materials and minerals. A public hearing has not been scheduled, but Treasury will do so if any interested party requests such a hearing in a timely written comment. In the meantime, the Proposed Regulations provide those in the clean vehicle industry with greater certainty as to the Excluded Entities Rule.



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings Los Angeles Lawyers:

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¹ IIA § 40207(a)(5) (citing (10 U.S.C. § 4872(d)(2)).

² “**Battery cell**” is defined in the Proposed Regulations as a combination of battery components (other than battery cells) capable of electrochemically storing energy from which the electric motor of a new clean vehicle draws electricity.