Energy sector tax provisions in “One Big Beautiful Bill”

KPMG analysis and observations

This report reflects the legislation signed into law by the president on July 4, 2025 (Pub. L. No. 119-21) and was last updated on July 21, 2025.

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Contents

Introduction

President Trump on July 4, 2025, signed into law the bill commonly referred to as the "One Big Beautiful Bill" (OB3), H.R. 1.

This document serves as a quick guide to the provisions in the legislation affecting the energy sector. The focus is particularly on clean energy initiatives, emphasizing the important changes to tax incentives and credits that are currently used to determine financing for those projects. KPMG analysis aims to provide clarity and actionable insights into how these provisions can impact those involved in these projects. A more detailed series of reports on the legislation can be found **here**.

Credits terminated

Enacted legislation (secs. 70501-70508)

The enacted legislation includes provisions that terminate certain tax credits and deductions as follows:

- Previously owned clean vehicle credit (section 25E) for vehicles acquired after September 30, 2025
- Clean vehicle credit (section 30D) for vehicles acquired after September 30, 2025
- Qualified commercial clean vehicle credit (section 45W) for vehicles acquired after September 30, 2025
- Alternative fuel vehicle refueling property credit (section 30C) for property placed in service after June 30, 2026
- Energy efficient home improvement credit (section 25C) for property placed in service after December 31, 2025
- Residential clean energy credit (section 25D) for expenditures made after December 31, 2025
- Energy efficient commercial buildings deduction (section 179D) for property beginning construction after June 30, 2026
- New energy efficient home credit (section 45L) for new homes acquired after June 30, 2026

KPMG observation

In general, the enacted legislation accelerates the termination of the electrical vehicle (EV) credits even faster than previous proposals to September 30, 2025. Interestingly, a colloquy on the House floor stated that this deadline could include commercial EVs acquired through a binding written contract by the deadline. The credit for EV charging stations fares slightly better, terminating for property placed in service after June 30, 2026. Residential energy efficiency credits terminate at the end of 2025. The energy efficient commercial buildings deduction, as well as the new energy efficient home credit, terminate after June 30, 2026.

Clean electricity production tax credit (PTC)

Pre-OB3 law

Under the law prior to OB3, section 45Y allows a PTC for electricity produced by the taxpayer at a qualified facility and sold to an unrelated person during the tax year. The credit is also available where the electricity is consumed or stored by the taxpayer if the facility is equipped with a metering device owned and operated by an unrelated person. The credit is available for electricity produced during a 10-year credit period beginning when the qualified facility is placed in service.

The base credit is 0.3 cents per kWh, and the credit amount is increased to 1.5 cents per kWh for facilities that have a maximum output of less than 1 MW of electricity, that meet certain prevailing wage and apprenticeship requirements, or that began construction prior to January 29, 2023. The credit amount is inflation-adjusted.

The credit amount is increased by 10% for qualified facilities located in an "energy community" and by an additional 10% for qualified facilities meeting certain domestic content requirements.

A qualified facility is an electricity generation facility in the United States owned by the taxpayer that is placed in service after 2024 and for which the greenhouse gas emissions rate is not more than zero. A qualified facility includes property placed in service after 2024 that expands the capacity of a facility placed in service prior to 2025, and a credit is available on the increased production.

The credit is phased out for facilities for which construction begins after the "applicable year," which is defined as the later of 2032, or the calendar year in which the Secretary determines that the annual greenhouse gas emissions from the production of electricity in the United States are equal to or less than 25% of the 2022 emissions. Qualified facilities for which construction begins in the year following the applicable year receive the full credit; qualified facilities for which construction begins in the second or third year following the applicable year will receive a reduced credit of 75% or 50%, respectively, of the credit amount; and qualified facilities for which construction begins more than three years after the applicable year will not be eligible for the credit.

The credit is transferable under the law prior to OB3, and certain tax exempt and government entities are eligible for direct pay.

To be eligible for the credit, tax-exempt and government entities are generally required to meet certain domestic content requirements for qualified facilities with net output of at least 1MW for which construction begins after 2025. For qualified facilities for which construction begins after 2023 and before 2026, a reduced credit is allowed.

Enacted legislation (sec. 70512)

The legislation retains the pre-OB3 phase-out schedule for qualified facilities other than wind and solar facilities, although it defines the "applicable year" as 2032 (i.e., it eliminates the potential for a later phase-out if the targeted emissions rate is met after 2032). This means that the phase-out of the credit for qualified facilities other than wind and solar will effectively start for facilities that begin construction in 2034.

For wind and solar facilities, the legislation generally terminates the credit so that qualified wind and solar facilities are not credit eligible unless they either begin construction within 12 months from enactment or if they are placed in service by December 31, 2027.

For purposes of determining the credit on increased production at a qualified facility, the legislation provides rules for determining capacity. The legislation also allows the use of existing studies for purposes of determining the greenhouse gas emissions rate of a qualified facility.

Further, the legislation denies the credit for small wind and solar water heating property leasing arrangements and expands it to include all such leases, rather than just leases to individuals.

Further, solely for purposes of the PTC, the legislation adds an additional category to the energy community credit increase. Specifically, it adds certain advanced nuclear facilities if located in a metropolitan statistical area with 0.17% or greater employment related to the advancement of nuclear power.

The legislation is generally effective for tax years beginning after the date of enactment.

KPMG observation

The requirement that wind and solar facilities begin construction before July 4, 2026, or be placed in service by December 31, 2027, compresses the timeline for credit eligibility. Further, while transferability was retained, KPMG expects that the beginning of construction and eventually the placed in service dates will be a significant focus of diligence efforts. It is important that proper contemporaneous documentation be maintained during the process. The Executive Order issued on July 7, 2025, further complicates the matter and is described in more detail below.

Prohibited foreign entity (PFE) rules

The legislation denies the credit for qualified facilities that begin construction after 2025 and receive **material assistance** from a prohibited foreign entity (PFE). Specifically, a qualified facility that begins construction after 2025 is required to have a material assistance cost ratio above the threshold percentage.

For a qualified facility that begins construction in 2026, the threshold percentage is 40% - meaning 60% of manufactured products (including components) could be directly or indirectly acquired from PFEs. The threshold percentage increases by 5% per year until it reaches 60% for qualified facilities beginning construction after 2029. The material assistance cost ratio is the percentage equal to (A) the total direct costs to the taxpayer attributable to all manufactured components which are incorporated into the qualified facility or energy storage minus (B) the total direct costs to the taxpayer attributable to all manufactured products (including components) which are mined, produced, or manufactured by a PFE, divided by (C) the total direct costs computed in (A).

For energy storage technology that begins construction in 2026, the threshold percentage is 55%. The percentage increases by 5% per year until it reaches 75% for energy storage that begins construction after 2029.

KPMG observation

While previous proposals would have made the section 45Y credit unavailable if even a single component, subcomponent, or critical mineral (directly or indirectly) produced by a PFE was used to construct the qualified facility, the enacted legislation allows manufactured products to be acquired from PFEs up to a threshold ratio. The threshold ratio is increased over time.

The legislation also denies the credit, in tax years beginning after enactment (July 4, 2025), if the taxpayer is itself a PFE, which is defined as a specified foreign entity or a foreign-influenced entity.

A **specified foreign entity** includes:

- Certain foreign entities of concern as described in the *William M. (Mac) Thornberry National Defense Authorization Act of FY 2021*
- Chinese military companies operating in the United States
- Any entity on a list required by the strategy to enforce prohibition on imported goods made through forced labor in the Xinjiang Uyghur autonomous region
- Any entity listed as ineligible for Department of Defense battery acquisition in the *National Defense Authorization Act of FY 2024*
- Foreign-controlled entities

A **foreign-controlled entity** includes:

- The government (including agencies and instrumentalities) of a covered nation (i.e., the Democratic People's Republic of North Korea; the People's Republic of China; the Russian Federation; and the Islamic Republic of Iran)
- A person who is a citizen, national or resident of a covered nation provided the person is not a US citizen or lawful permanent resident
- An entity or qualified business unit incorporated or organized under the laws of or having its principal place of business in a covered nation
- An entity controlled by a foreign-controlled entity

For purposes of determining whether an entity is a foreign-controlled entity, control would generally be defined as a greater than 50% ownership of the stock of a corporation, the profits or capital interests of a partnership, or the beneficial interests in any other entity.

A **foreign-influenced entity** is defined as an entity which, during the tax year, has:

- A specified foreign entity that has the direct or indirect authority to appoint a covered officer
- A single specified foreign entity that owns at least 25%, or if one or more specified foreign entities own in the aggregate at least 40% of such entity or hold at least 15% of the entity's debt

Further, an entity may be a foreign influenced entity if, during the previous tax year, it made a payment to a specified foreign entity pursuant to an agreement that entitles the specified foreign entity (or a related entity) to exercise *effective control* over a qualified facility or an energy storage technology (for energy storage technology, this is relevant under the clean electricity ITC discussed in the next section). The legislation generally provides that a contractual counterparty has effective control when it has specific authority over key aspects of the production of energy generation in a qualified facility, or energy storage. With respect to payments exercising effective control, the credit is disallowed only if the payments made are related to the qualified facility or energy storage property. The legislation authorizes Treasury to provide guidance and specifies rules that are required to be followed in the interim.

The legislation includes special rules that prevents certain publicly traded entities from being classified as a foreign-controlled or a foreign-influenced entity under the applicable rules.

Additionally, for tax years beginning after enactment, the enacted legislation prohibits the transfer of any portion of the credit to specified foreign entities.

KPMG observation

The introduction of the PFE rules will introduce a complex regime requiring taxpayers to pay close attention to the ultimate ownership of taxpayers claiming the credit and the sourcing of the materials used for a project.

Further, the effective date of these provisions is anchored to the beginning of construction as provided in a series of Notices including 2013-29 and 2018-59, which is likely going to be inconsistent with the beginning of construction for general credit qualification purposes. As of this writing, there is no guidance on the meaning of beginning of construction for general credit qualification purposes.

Clean electricity investment tax credit (ITC)

Pre-OB3 law

Taxpayers may claim an ITC under section 48E for any qualified facility or energy storage technology placed in service in a tax year. A qualified facility is generally defined as depreciable tangible property with a placed-in-service date after 2024 that is used for the generation of electricity and that has a greenhouse gas emissions rate no greater than zero. A qualified facility also includes certain interconnection property.

The base ITC rate is 6%, and the rate is increased to 30% for facilities that have a maximum net output of less than 1 MW of electricity, that meet certain prevailing wage and apprenticeship requirements, or that began construction prior to January 29, 2023.

Potential credit increases are available for placing the facility in service in an energy community or meeting certain domestic content thresholds.

Currently, the credit begins to phase out in the “applicable year,” which is defined as the later of 2032, or the calendar year in which the Secretary determines that the annual greenhouse gas emissions from the production of electricity in the United States are equal to or less than 25% of the 2022 emissions.

The credit is transferable under pre-OB3 law, and certain tax exempt and government entities are eligible for direct pay.

Enacted legislation (sec. 70513)

The legislation retained the pre-OB3 phase-out schedule for qualified facilities other than wind and solar facilities, and for energy storage technology, although it determines the “applicable year” to be 2032 (i.e., it eliminates the potential for a later phase-out if the targeted emissions rate is met after 2032). This means that the phase-out of the credit for qualified facilities other than wind and solar will effectively start for facilities that begin construction in 2034.

For wind and solar facilities, the legislation terminates the credit so that qualified wind and solar facilities will not be eligible unless they begin construction within 12 months from enactment or if they are placed in service by December 31, 2027

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The legislation increases the percentage of domestic content required to qualify for the domestic content adder, as follows:

- For projects that begin construction after June 16, 2025, and prior to 2026, 45% (27.5% for offshore wind)
- For projects that begin construction in 2026, 50% (35% for offshore wind)
- For projects that begin construction after 2026, 55%

The change is effective for qualified facilities and energy storage technology for which construction begins after June 16, 2025.

The legislation denies the ITC for lessors of small wind and solar water heating property and expands it to exclude all such leased property, rather than just leases to individuals. This provision is effective for tax years beginning after the date of enactment.

Additionally, the legislation adds a provision allowing qualified fuel cell property to qualify for the 30% credit, without meeting the greenhouse gas emissions rate requirements. The 30% credit rate cannot be increased for being placed in service in an energy community or meeting the domestic content requirements. Further, the credit rate is not dependent on meeting prevailing wage and apprenticeship requirements. This rule is effective for facilities beginning construction after 2025.

PFE rules: The legislation provides PFE rules for the section 48E ITC that are generally the same as those provided for the section 45Y PTC. Under those rules, the credit is denied for qualified facilities, qualified interconnection property, or energy storage property that begins construction after 2025 and receives material assistance from a PFE.

The credit is also denied in tax years beginning after enactment (July 4, 2025) if the taxpayer is itself a PFE. Additionally, for tax years beginning after enactment (July 4, 2025), the legislation prohibits the transfer of any portion of the credit to specified foreign entities. (See discussion in the section 45Y portion of this booklet for a full discussion of the PFE rules.)

Recapture rule: The legislation requires 100% recapture of the clean electricity ITC if an "applicable payment" is made by a specified taxpayer during the 10-year window beginning with the placed in service date of a qualified facility or energy storage technology. An applicable payment is defined as a payment to a specified foreign entity pursuant to an agreement entitling that entity to exercise effective control over a qualified facility or energy storage technology owned by the taxpayer. This recapture provision applies to credits allowed in tax years beginning after July 4, 2027, more than two years after enactment.

Executive Order

On July 7, 2025, an Executive Order was released that directs to Treasury Secretary to issue guidance within 45 days (by August 21, 2025) "to ensure that policies concerning the 'beginning of construction' are not circumvented" in the case of sections 48E and 45Y. Specifically, the order directs that such guidance prevent "artificial acceleration or manipulation of eligibility" and restrict the use of "broad safe harbors unless a substantial portion of a subject facility has been built."

KPMG observation

The enacted legislation requiring wind and solar projects to begin construction within 12 months of enactment or be placed in service by 2027 is easier to handle than an earlier draft of the bill, but the legislation will still have a monumental effect on the wind and solar industry.

The introduction of the PFE rules will introduce a complex regime requiring taxpayers to pay close attention to the ultimate ownership of taxpayers claiming the credit and the sourcing of the materials used for a project.

Further, the effective date of these provisions is anchored to the beginning of construction as provided in a series of Notices including 2013-29 and 2018-59 which is likely going to be inconsistent with the beginning of construction for general credit qualification purposes. As of this writing, there is no guidance on the meaning of beginning of construction for general credit qualification purposes.

Clean fuel production tax credit

Pre-OB3 law

Under the pre-OB3 law, section 45Z provides for an income tax credit for clean transportation fuel produced in the United States after 2024 and sold before 2028. Eligible fuels are generally classified as either sustainable aviation fuel (SAF) or non-SAF transportation fuel.

To qualify for the credit in a given tax year, taxpayers must produce the qualifying "transportation fuel" within the United States for sale to an unrelated person for certain specified purposes. Generally, a non-SAF transportation fuel cannot be produced using certain feedstocks, must be suitable for use in a highway vehicle or aircraft, and must have a lifecycle greenhouse gas (GHG) emissions rate of no greater than 50kg $CO2$ per mmBTU.

In addition, SAF must meet certain industry specifications and additional feedstock requirements and be sold for use in an aircraft.

A taxpayer calculates its section 45Z credit by multiplying the volume of qualifying fuel produced (in gallons or gallon equivalent) by a base rate, referred to as the "applicable amount," and an "emissions factor." The applicable amount is $0.20 for non-SAF transportation fuel and $0.35 for SAF (or $1.00 and $1.75, respectively, if the taxpayer satisfies prevailing wage requirements under section 45). The "applicable amount" is inflation-adjusted for years after 2024. The "emissions factor" is inversely proportional to the lifecycle GHG emissions potential of the fuel produced. A given fuel's lifecycle GHG emissions are determined using an emissions rate computed using an emissions model as provided for by guidance, including a table listing fuels and feedstock published annually by the Treasury (the "Annual Table").

KPMG observation

The legislation may be viewed favorably by the clean fuels industry, especially the extension of the credit. It also appears that the amendments for standardizing the emissions rates with respect to the ILUC and animal manure will provide more certainty to taxpayers who are required to calculate estimates.

However, the provision to exclude feedstocks not produced in the United States, Mexico, or Canada may require taxpayers to rethink where they source their feedstocks.

Enacted legislation (sec. 70521)

The legislation provides for a two-year extension of the clean fuel production credit for transportation fuel sold through 2029.

The final legislation limits credit eligibility to fuel produced from feedstocks from the United States, Mexico, or Canada, but for fuel *produced* after December 31, 2025.

Additionally, this legislation prohibits "double credits" by disallowing the credit for any fuel produced from another fuel for which a credit under section 45Z is allowable.

With respect to determining the emissions rate of a transportation fuel, the legislation prohibits negative emissions rates for such fuel produced after 2025.

The final legislation directs the Secretary to publish unique emissions rates for different animal manure feedstocks, permitting a negative rate in this instance.

The Secretary is authorized to issue rules related to the sale of fuel to related persons other than in the manner contemplated under section 52(b).

With respect to Sustainable Aviation Fuel (SAF), the final legislation:

- Terminates the section 6426(k) sustainable aviation fuel excise tax credit effective September 30, 2025.
- Reduces the section 45Z credit for SAF by an amount equal to any credit claimed under section 6426(k)(1) for SAF sold after 2024 and prior to October 1, 2025.
- Removes the higher special rate for SAF, creating parity with non-SAF transportation fuels under 45Z after 2025.

The legislation additionally extends and modifies the Small Agribiodiesel Producer Credit under section 40A(b)(4). A credit at a rate of 20 cents per gallon of fuel produced will be available through December 31, 2026. This provision allows stacking with a credit determined under 45Z. Additionally, transfer under section 6418 is permitted for credit generated under section 40A(b)(4).

PFE rules: The legislation denies the credit to specified foreign entities in tax years beginning after July 4, 2025, and to foreign-influenced entities in tax years beginning after July 4, 2027, more than two years after date of enactment. However, in determining whether a taxpayer is a foreign-influenced entity, it does not apply a certain provision in the “effective control” rules of amended section 7701(a)(51)(D)(i)(II) related to payments yielding “effective control” over PTC or ITC property to a specified foreign entity.

The legislation does not universally disallow transferability but does disallow transferability to specified foreign entities for tax years beginning after enactment (July 4, 2025).

KPMG observation

The clean fuel credits were not significantly reduced or altered by this legislation, with the exceptions to the SAF modifications. And additional guidance regarding the calculations of emissions rates and related party sales will be helpful in providing more certainty to taxpayers currently addressing these issues.

The legislation’s exclusion feedstocks not produced in the United States, Mexico, or Canada may require taxpayers to rethink where they source their feedstocks.

Credit for carbon oxide sequestration

Pre-OB3 law

Under pre-OB3 law, section 45Q allows credits to taxpayers who capture and sequester qualifying carbon oxide. The credit amount depends on a number of variables, including how the captured carbon oxide is used and whether the taxpayer met the prevailing wage and apprenticeship requirements during the construction, alteration or repair of the facility.

The credit is available for projects for which construction begins prior to 2033, and the current credit rates are as follows:

- Secure geological storage: Base credit rate of $17; bonus credit rate of $85 per metric ton
- EOR projects or utilization: Base credit rate of $12; bonus credit rate of $60 per metric ton
- Direct air capture (secure storage): Base rate of $36; bonus rate of $180 per metric ton
- Direct air capture (EOR/utilization): Base rate of $26; bonus rate of $130 per metric ton

To claim the section 45Q credit at the bonus credit rate, taxpayers must satisfy the:

- Prevailing wage requirement for the 12-year credit period
- Apprenticeship requirements during the construction of the project

The minimum capture thresholds under section 45Q are as follows:

- Direct air capture facilities must capture no less than 1,000 metric tons of carbon oxide per year
- Electricity generating facilities must capture no less than 18,750 metric tons of carbon oxide and, with respect to any carbon capture equipment for the applicable electric generating unit, have a capture design capacity of not less than 75% of baseline carbon oxide production
- Other industrial facilities must capture no less than 12,500 metric tons of carbon oxide

For carbon capture equipment placed in service after 2022, the section 45Q credit is eligible for the direct pay election, making it one of three credits deemed as refundable, regardless of whether the taxpayer is an applicable entity. This is available to the taxpayer for the first five years that the facility is in service.

Taxpayers may also elect, annually, to transfer the credit (or any portion of the credit) to an unrelated taxpayer for cash consideration.

Enacted legislation (sec. 70522)

While the pre-OB3 law allows a lesser benefit at the inflation-adjusted amount of $12/$60 for carbon captured and used as a tertiary injectant in enhanced oil recovery (EOR) or utilized in a commercial product or process, the enacted legislation increases the credit rate to $17/$85 for these uses to correspond to the secure geological storage credit rate for facilities placed in service subsequent to enactment.

PFE rules: The enacted legislation disallows a benefit under section 45Q for specified foreign entities (as described under proposed section 7701(a)(51)(B)), and foreign-influenced entities (as described under proposed section 7701(a)(51)(D)) for tax years beginning after July 4, 2025. However, the legislation does not apply a certain provision in the “effective control” rules of proposed section 7701(a)(51)(D)(i)(II) related to payments pursuant to agreements yielding “effective control” over PTC or ITC property to a specified foreign entity.

While transferability is not universally repealed, it does disallow transfers to specified foreign entities upon enactment.

KPMG observation

The final legislation largely retains the structure and rates for the section 45Q credit for projects that begin construction prior to 2033. Carbon capture technology is capital intensive, so this is welcome news to taxpayers investing in this technology. In addition, the retention of the direct pay rules maintains a useful monetization option for these projects.

Additionally, the legislation brings parity with the different storage options for carbon oxide captured, increasing the credit rate for carbon captured and used in EOR or utilized in a commercial product or process.

Lastly, as mentioned in other observations, the introduction of the FEOC restrictions may require taxpayers to consider particularly complex rules and the legal structures in which these projects reside.

Zero-emission nuclear power production credit

Pre-OB3 law

Section 45U provides, for tax years beginning after 2023, a production tax credit for the production and sale of nuclear power from an existing qualified nuclear power facility. The credit is not available for tax years beginning after 2032.

The credit can be transferred or sold to third parties.

Enacted legislation (sec. 70510)

The legislation denies the section 45U credit to specified foreign entities in tax years beginning after July 4, 2025, and to foreign-influenced entities in tax years beginning after July 4, 2027, more than two years after enactment.

In addition, elective transfers of the credit are denied in tax years beginning after July 4, 2025, if the transferee is a specified foreign entity (as defined in section 7701(a)(51)(B)).

KPMG observation

The zero-emission nuclear power production credit remained generally unscathed compared to the pre-OB3 law in this final legislation.

Credit for production of clean hydrogen

Pre-OB3 law

Under pre-OB3 law, the section 45V credit provides for a production tax credit that is generally determined based on the amount of clean hydrogen produced during the 10-year period following the date the production facility is placed in service, and the emissions intensity of the process used to produce the hydrogen.

To be eligible, the hydrogen produced must have emissions of 4 kg of CO_2e per kg of hydrogen produced or less, and the credit amount is higher when the hydrogen production process' emissions are lower. The maximum credit rate is $3/kg of hydrogen produced. In lieu of the clean hydrogen production tax credit, a taxpayer can elect to treat the facility (or a portion of the facility) as energy property under section 48. (The energy percentage ranges from 1.2 to 6% base rate and 6 to 30% bonus rate depending on the type of clean hydrogen that is produced.)

A qualified clean hydrogen facility must currently begin construction by December 31, 2033, to be eligible for the clean hydrogen production credit.

For qualified clean hydrogen production facilities placed in service after 2022, taxpayers may elect to receive a direct payment of this credit. Such an election must be made separately with respect to each facility, be made for the tax year in which the facility is placed in service (or within one year of the date of enactment) and applies to such tax year and four subsequent tax years. Such an election may only be made with respect to any tax years beginning before 2033.

In addition, a taxpayer may elect to transfer the credit (or any portion of the credit) to an unrelated taxpayer and exclude such sale proceeds from gross income. For any tax years for which a direct pay election is made, taxpayers may also not elect to transfer the credit. The election for transferability must be made annually and with respect to each facility for which the credit is determined.

Enacted legislation (sec. 70511)

The enacted legislation terminates the credit for facilities the construction of which begins after December 31, 2027.

KPMG observation

Initial proposals, including the House bill, called for a termination of this credit for facilities that begin construction after 2025. The final legislation was a win for the hydrogen industry, as it adds two years on the life of this credit, terminating the credit for facilities that begin construction after 2027. Given the complexity of these projects, this is a welcome development for the industry.

Enhancement of advanced manufacturing investment credit

Pre-OB3 law

Eligible taxpayers are allowed a credit under section 48D equal to 25% of qualified property placed in service in a tax year that is part of an advanced manufacturing facility. An advanced manufacturing facility is generally defined as a facility with the primary purpose of manufacturing semiconductors or semiconductor manufacturing equipment.

The credit is not available for qualified property for which construction begins after 2026.

Enacted legislation (sec. 70308)

The enacted legislation increases the credit rate to 35% for property placed in service after 2025. It does not modify the requirement that construction must begin before 2026.

KPMG observation

While the legislation increases the credit to 35% for qualified property placed in service after 2025, it does not address the treatment of qualified progress expenditures. Taxpayers that have elected to claim the credit on qualified progress expenditures in the year such expenditures are incurred, rather than claiming the credit to the placed-in-service-date year, will presumably claim a 25% credit rather than a 35% credit, even if the qualified property is placed in service after 2025.

Advanced manufacturing production credit

Pre-OB3 law

Under pre-OB3 law, section 45X provides a production credit for the U.S. production and sale of certain eligible components. These components include wind, battery, and solar components, as well as certain "critical minerals" supporting these supply chains. The production of most eligible components phases out starting after 2032; there is no phase-out for the production of critical materials. Generally, the credit is claimed in the year the eligible component is sold.

Enacted legislation (sec. 70514)

The final legislation provides for three major modifications to section 45X.

- Modifies the phaseout of the credit
- Adds metallurgical coal as a critical mineral under the credit
- Provides that production facilities that have certain forms of non-U.S. ownership or receive material assistance from a prohibited foreign entity (PFE) are no longer be eligible for the credit

Phaseout modification

Under the legislation, wind energy components sold after 2027 are not eligible for a credit.

The legislation limits the ability of taxpayers to stack credits where they are manufacturing multiple eligible types of eligible components. To qualify for the integrated component rule for tax years beginning after 2026, an eligible component (the "primary component") must be integrated into another eligible component (the "secondary component") produced in the same facility, and the secondary component must have at least 65% of its direct material costs attributable to primary components produced in the US and must be sold to an unrelated party.

Additionally, the credit for "critical minerals" has a staggered phaseout beginning with critical minerals produced in 2031.

Metallurgical coal

The final legislation adds metallurgical coal to the list of applicable critical minerals for tax years beginning after July 4, 2025. No credit is available related to production of metallurgical coal after December 31, 2029. The credit amount is 2.5% of production costs.

Prohibited foreign entity rules

The section 45X credit is unavailable to a PFE for tax years beginning after July 4, 2025.

Additionally, a material assistance provision is provided for tax years beginning after July 4, 2025. Producers must have a material assistance cost ratio greater than the threshold percentage below:

- Solar energy components – 50% in 2026, 60% in 2027, 70% in 2028, 80% in 2029 and 85% thereafter
- Wind energy components – 85% in 2026, 90% in 2027
- Inverters – 50% in 2026, 55% in 2027, 60% in 2028, 65% in 2029, and 70% thereafter
- Battery energy components – 60% in 2026, 65% in 2027, 70% in 2028, 80% in 2029, and 85% thereafter
- Critical minerals – 2026-2029, no restrictions, 25% in 2030, 30% in 2031, 40% in 2032, and 50% in 2033 and thereafter (subject to adjustment by the Secretary based on availability in the United States, national security, and supply chain constraints)

The material assistance cost ratio is a fraction equal to (A) total direct material costs paid or incurred (defined under section 263A) by the taxpayer for production of an eligible component minus (B) total direct material costs paid for incurred by the taxpayer for production of an eligible component that are mined, produced, or manufactured by a PFE, (C) divided by the total direct costs in (A).

Further, the enacted legislation does not disallow transfers of a 45X credit, except for the transfer of a credit to a specified foreign entity. Those transfers are disallowed upon enactment.

KPMG observation

The introduction of the PFE and material assistance rules to the section 45X credit could prove challenging for taxpayers. The enacted legislation disallows the credit based on the percentage of materials in a component that were acquired from a PFE, with the percentage increasing over time, attempts to allow more time for U.S. supply chains to be built.

Restriction on the extension of advanced energy project credit program

Pre-OB3 law

Section 48C provides an allocated credit for qualified investments in qualifying advanced energy projects. The credit is allowed in the year the property constituting the qualified investment is placed in service.

Credits are allocated to the sponsors of qualifying advanced energy projects through a qualifying advanced energy project program established by Treasury. The total amount of credits available for allocation under the program is $10 billion.

Recipients of an allocation have two years to place the project into service. If this placed-in-service date requirement is not met, the allocation to that recipient is revoked and the amount of the allocation may be reallocated to one or more different recipients by Treasury.

Enacted legislation (sec. 70515)

The enacted legislation provides that any section 48C credit allocation amounts that are revoked will not be reallocated to a different recipient.

This provision is effective upon enactment.

Expansion of the definition of qualifying income of certain publicly traded partnerships treated as corporations

Pre-OB3 law

Under present law, a publicly traded partnership generally is treated as a corporation for federal tax purposes. An exception from corporate treatment is provided for certain publicly traded partnerships, if 90% or more of the gross income of the publicly traded partnership is "qualifying income."

Qualifying income includes interest, dividends, and gains from the disposition of a capital asset (or of property described in section 1231(b)) that is held to produce qualifying income. Qualifying income also includes rents from real property, gains from the sale or other disposition of real property, and income and gains from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resource (including fertilizer, geothermal energy, and timber), industrial source carbon dioxide, or the transportation or storage of any alcohol fuel mixture, biodiesel fuel mixture or alternative fuel described in subsection (b), (c), (d), or (e) of section 6426, or any alcohol fuel defined in section 6426(b)(4)(A) or any biodiesel fuel as defined in section 40A(d)(1). It also includes income and gains from commodities (not described in section 1221(a)(1)) or futures, options, or forward contracts with respect to such commodities (including foreign currency transactions of a commodity pool) in the case of a partnership, a principal activity of which is the buying and selling of such commodities, futures, options or forward contracts

Enacted legislation (sec. 70524)

The final legislation expands the definition of qualifying income of a publicly traded partnership to include:

- Income and gains with respect to the transportation or storage of sustainable aviation fuel as described in section 40B(d)(1),
- Income and gains with respect to the transportation or storage of liquified hydrogen or compressed hydrogen,
- Income and gains with respect to the generation, availability for such generation, or storage of electric power, or the capture of carbon dioxide by a "qualified facility" whose total carbon oxide production is at least 50% "qualified carbon oxide,"
- Income and gains with respect to the production of electricity from any advanced nuclear facility (as defined in section 45J(d)(2)),
- Income and gains with respect to the production of electricity or thermal energy exclusively using a geothermal energy resource or a qualified hydropower production resource as described in sections 45(c)(1)(D) or (H), and
- Income and gains with respect to the operation of geothermal energy property described in sections 48(a)(3)(A)(iii) or (vii) (determined without regard to any requirement under such section with respect to the date on which construction of property begins).

The legislation applies to tax years beginning after 2025.

Modification of limitation on business interest

Pre-OB3 law

The deduction for business interest expense is limited to 30% of the sum of adjusted taxable income (ATI), business interest income and floor plan financing interest. Under present law, ATI is calculated in a manner similar to earnings before interest and taxes (generally referred to as “EBIT”). The term “floor plan financing interest” means interest paid or accrued on indebtedness used to finance the acquisition of motor vehicles held for sale or lease and secured by the inventory so acquired. For this purpose, the term “motor vehicle” includes (1) a self-propelled vehicle designed for transporting persons or property on a public street, highway, or road, (2) a boat, or (3) farm machinery or equipment. Thus, under present law, towed trailers and campers that are not self-propelled vehicles do not qualify as a "motor vehicle." Under present law, any taxpayer which meets the gross receipts test of section 448(c) (other than a tax shelter) is not subject to the interest expense limitation under section 163(j).

Enacted legislation (sec. 70303)

The final legislation reinstates the determination of ATI in a manner similar to EBITDA (i.e., without regard to the allowance for depreciation, amortization, or depletion), permanently for tax years beginning after December 31, 2024.

KPMG observation

Capital intensive businesses were disproportionately impacted by the switch from an EBITDA to EBIT approach to calculating ATI for tax years beginning after 2021. Reverting to an EBITDA increases affected taxpayers’ interest deductions for the years impacted. Coupled with the extension of 100% bonus depreciation and the special depreciation allowance for qualified production property, manufacturers and other taxpayers with large capital spend could see a significant increase in the amount of business interest allowed to be deducted. There were no changes to the provisions that require or allow certain taxpayers with certain utility operations to be exempt from the section 163(j) provisions.

Taxpayers who would benefit from the legislation but are subject to the base erosion tax under section 59A (BEAT) should model the potential interactions with their BEAT calculations. For example, an increase in the amount of interest deductible under section 163(j) could in turn increase a taxpayer’s base erosion tax benefits under section 59A if such interest was paid or accrued to a foreign related party. In addition, lower regular tax liability because of increased deductions for interest could negatively impact a taxpayer’s BEAT liability. For more information, read the International Tax report located on KPMG’s dedicated webpage.

The definition of depreciation and amortization for purposes of section 163(j) is expansive and includes most types of cost recovery over time, including the amortization of various intangibles (e.g., under section 174 (or proposed section 174A), 167, 195, 197, 248, etc.). Thus, taxpayers should also model the impact of the proposed full expensing of domestic R&E expenditures on their ATI calculation. Amortization of R&E expenditures capitalized under section 174 and/or proposed section 174A(c) would be added back in calculating ATI while amounts that are fully deducted in the year paid or incurred would not. Taxpayers with significant business interest and R&E expenditures may benefit by electively capitalizing domestic R&E expenditures under section 174A. Applicable corporations subject to CAMT will also want to model the interactions of an increased interest expense deduction on any potential CAMT liability. Decreased taxable income may result in a CAMT liability for applicable corporations and, as a result, a CAMT credit that may or may not be useable in future tax years.

Reinstatement of 100% bonus depreciation

Pre-OB3 law

The TCJA temporarily increased the section 168(k) first-year “bonus” depreciation deduction to 100%, allowing taxpayers to write off immediately the cost of qualified property when placed in service. The 100% bonus depreciation rate applied through 2022 and then started ratably phasing down over the succeeding five years. Thus, the bonus depreciation percentage under section 168(k) is generally 80% for property placed in service in 2023, 60% for property placed in service in 2024, and 40% for property placed in service in 2025. The percentage will continue to decrease to 20% for 2026 and expire in 2027. Similarly, section 168(k)(5) provides a special election to deduct the applicable bonus depreciation percentage of the costs of planting or grafting specified plants during such years (rather than in the year the specified plant is placed in service by the taxpayer).

While the bonus depreciation percentage generally decreased to 60% for assets placed in service in 2024 (and decreases to 40% for assets placed in service in 2025), certain qualified property placed in service in 2024 remains eligible for the 80% deduction (and if placed in service in 2025 will remain eligible for the 60% deduction). To be eligible for this extended placed-in-service date rule, an asset must meet all of the requirements of section 168(k)(2)(A)(i) and (ii), have a recovery period of at least 10 years or constitute transportation property, and constitute longer production period (“LPP”) property. LPP property must have either (1) a production period in excess of two years; or (2) a cost in excess of $1 million and a production period in excess of one year. Examples of assets that may qualify include pipelines, barges and other vessels, and power generation facilities.

A corporate aircraft (i.e., an aircraft that is not used in the business of transporting people or freight) is also eligible for the extended placed-in-service date rule so long as the aircraft is acquired by purchase and the purchaser made a non-refundable deposit of the lesser of $100,000 or 10% of the purchase price. In addition, the aircraft must have a production period of more than four months and a cost in excess of $200,000.

KPMG observation

Because otherwise qualifying property acquired prior to January 20, 2025, would continue to be subject to the current-law, phased-down bonus percentages, taxpayers would benefit from evaluating acquisitions occurring in late 2024 and early 2025 to determine whether the acquisition may be treated as occurring after January 19, 2025. Even if an asset is determined to be acquired prior to January 20, 2025, taxpayers would presumably be able to apply the elective component rules under existing Treasury regulations to qualify components acquired after January 19, 2025, as eligible for the 100% bonus depreciation deduction.

Should the proposal pass as drafted, taxpayers may benefit from the administrative simplicity of the law given that this provision does not include phase-down percentages to plan around or a retroactive date that could burden taxpayers to amend previous tax returns or file accounting method changes.

Similarly to when the bonus depreciation rate was increased to 100% under the TCJA, this provision could have an important effect on M&A transactions. It would increase the incentive for buyers to structure taxable acquisitions as actual or deemed (e.g., pursuant to section 338) asset purchases, rather than stock acquisitions, by enabling the purchasing entity in an asset acquisition to immediately deduct a significant component of the purchase price, and potentially generate net operating losses in the year of acquisition that could be carried forward to shield future income.

Increased bonus depreciation may have an impact on a corporation's future applicable corporation status for CAMT purposes. Although taxpayers are generally permitted to deduct tax depreciation in computing their adjusted financial statement income (AFSI), which yields a favorable result in years in which bonus depreciation is claimed, the inverse may be true in future tax years where property is fully depreciated and no tax depreciation deduction is available. Corporations that are not currently applicable corporations subject to CAMT but anticipate coming under the regime in a future year might want to model the effect on future tax years if 100% bonus depreciation is claimed in a year prior to being subject to CAMT, including modeling the effects of electing out of bonus depreciation for certain classes of property to extend tax depreciation deductions (and favorable CAMT adjustments) into future CAMT years. Further, when 100% bonus depreciation is coupled with the section 163(j) and section 174A proposals, the impact on taxable income (and any potential CAMT liability) could be material.

Enacted legislation (sec. 70301)

The enacted legislation permanently reinstates the 100% additional first-year depreciation deduction under section 168(k), for qualified property acquired after January 19, 2025, and specified plants planted or grated after such date. For acquisition date determinations, the enacted legislation prohibits qualified property from being treated as acquired after the date on which a written binding contract is entered into for such acquisition.

As part of making 100% bonus depreciation permanent, the legislation removes the limitation for self-constructed property under pre-OB3 law that requires self-constructed property to be manufactured, constructed, or produced before 2027. Similarly, there is no requirement that qualified property be placed in service before 2027 (before 2028 in the case of LPP property and certain aircraft), as well as the requirement that specified plants be planted or grafted before 2027.

The legislation provides a transitional election, whereby taxpayers can apply a reduced bonus depreciation percentage of 40% for qualified property (60% for LPP property and certain aircraft) placed in service by the taxpayer during the first tax year ending after January 19, 2025, in lieu of the 100% bonus depreciation percentage that would otherwise apply. Similarly, a transitional election is available to apply a bonus depreciation percentage of 40% (in lieu of 100%) to specified plants planted or grafted by a taxpayer during its first tax year ending after January 19, 2025.

KPMG observation

Certain transactions and purchases of property will need to be closely scrutinized to determine if the property was acquired after January 19, 2025 as that determination may not be as straight-forward as it would seem. This provision hinges on the acquisition date, not the placed in service date.

For fiscal year taxpayers with tax years ending shortly after January 19, 2025, the transitional election provides administrative ease by allowing the use of current bonus depreciation deduction percentages for taxpayers that might not want to recalculate depreciation for the first tax year ending after January 19, 2025. Presumably the election is meant to be limited to tax years ending after January 19, 2025, that include January 20, 2025, similar to what applied under current law to property placed in service during a taxpayer's first tax year ending after September 27, 2017, that included September 28, 2017 (see section 168(k)(10) and Treas. Reg. § 1.168(k)-2(f)(3), providing a transitional election to use the pre-TCJA 50% bonus depreciation rate for such tax year).

As discussed above, the permanency of 100% bonus depreciation coupled with the section 163(j) EBITDA approach, and section 174A expensing for U.S. research expenditures makes modeling the impact of each of the provisions on taxable income and any potential CAMT liability, as well as the interaction with numerous international tax rules including the section 250 deduction for FDII and GILTI, and foreign tax credit capacity, even more important.

The legislation applies to property acquired after January 19, 2025, and specified plants planted or grafted after such date. In the case of the transitional election of a reduced bonus depreciation percentage, the enacted legislation applies to tax years ending after January 19, 2025.

Coordination of business interest limitation with interest capitalization provisions

Pre-OB3 law

Under pre-OB3 law, the Code provides no ordering rule for coordinating the interest limitation rules under section 163(j) with other provisions of the Code under which business interest expense may be capitalized. Regulations promulgated under section 163(j) provide a coordination rule indicating that business interest capitalized under a provision that subjects interest to capitalization is not subject to the section 163(j) limitation.

Enacted legislation (sec. 70341)

The legislation provides an ordering rule that subjects interest that is capitalized under any provision other than section 263(g) or section 263A(f) to the limitation and further provides that the amount of business interest expense allowable after the application of the business interest expense limitation is applied to otherwise capitalized business interest expense before any other business interest expense.

The legislation also provides that any business interest expense disallowed under section 163(j) in a prior year and subsequently carried forward shall not be treated as interest to which any interest capitalization provision applies.

Lastly, the legislation provides the IRS with authority to issue regulations or other guidance as necessary, including regulations or guidance to determine which business interest is taken into account under sections 163(j) and 59A(c)(3). The legislation is applicable for tax years ending after December 31, 2025.

KPMG observation

The ordering rule in the final legislation adds additional complexity to the application of section 163(j) by adding another step in the determination of the taxpayer's current deduction for business interest expense and does not completely eliminate a potential circularity issue in cases where the amount of interest capitalized exceeds the amount of interest otherwise allowable after applying the limit.

Termination of five-year cost recovery for energy property

Pre-OB3 law

Under pre-OB3 law, section 168(e)(3)(B) lists specific categories of assets that are five-year property for MACRS purposes. Under section 168(e)(3)(B)(vi)(I), this list includes any property described in section 48(a)(3)(A) (applied by substituting “solar or wind energy” for “solar energy” in section 48(a)(3)(A)(i) and disregarding the last sentence of section 48(a)(3)). Thus, for example, this five-year property class includes assets such as equipment using solar or wind energy to generate electricity (e.g., solar panels).

The legislation strikes section 168(e)(3)(B)(vi)(I) from the Code, removing energy property from being five-year recovery property for purposes of section 168, unless such property is described in another category of section 168(e)(3)(B) or properly included in an asset class of Rev. Proc. 87-56, 1987-2 C.B. 674, that has a five-year MACRS recovery period.

This provision is effective for property the construction of which begins after December 31, 2024.

KPMG observation

The removal of wind and solar energy property from the statutory five-year property class will cause taxpayers engaged in such activities to need to determine which asset class will otherwise apply to such assets. Combined with the permanent reinstatement of 100% bonus depreciation, this change might not have a significant impact on a taxpayer’s depreciation deduction (e.g., if the otherwise applicable asset class would provide a MACRS recovery period of 20 years or less). However, depending on the activity in which an asset is used, some of these assets might no longer be eligible for bonus depreciation (e.g., if it would have a MACRS recovery period of more than 20 years). Further, since many states decouple from the federal bonus depreciation deduction, this change could impact taxpayers’ state income tax liabilities.

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