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# Considering a New or Pre-Owned Electric Vehicle? Read This First to See If You Will Benefit From a Tax Credit

2023 brings with it a whole new set of rules related to qualifying for the tax credit for purchasing a new or used electric vehicle. Among the changes that must be navigated are buyer income limitations, vehicle assembly and component limitations and even vehicle price caps.

So before you purchase a vehicle with the expectation that you will qualify for a tax credit, and whether that tax credit will really provide any financial benefit, you may find it appropriate to first review all the limits.

**MAGI Limit -** The first thing to determine is if your income is too high to claim a credit. If it is, you need not read any further since you won't qualify for the credit.

Even this gets a little tricky because the tax code allows you to base the income qualification on either your current year (year you buy the vehicle) or the prior year. The reason the law was written that way is to provide some level of certainty since the current year's income is uncertain, while the prior year's is already known.

Making things even more complicated, your income is measured by your modified adjusted gross income (MAGI). Generally an individual's MAGI is the same as their adjusted gross income (AGI) which appears on line 11 of your 2022 1040 or 1040-SR. However, some individuals may have excluded foreign or possessions income which must be added back to arrive at their MAGI.

Thus to qualify for a credit, a taxpayer's MAGI for the year of purchase OR the previous year must not exceed the amounts shown in the following table.

| MAGI LIMIT | | |
|---|---|---|
| Buyer's Filing Status | For the Purchase of a: | |
| | New Clean Vehicle, Hybrid or Fuel Cell Vehicle | Previously Owned Clean Vehicle |
| Married Taxpayers Filing Jointly or Qualifying Surviving Spouse | $300,000 | $150,000 |
| Head of Household | $225,000 | $112,500 |
| All Other Filing Statuses | $150,000 | $75,000 |

If your MAGI is equal to or less than the limit, then you may qualify for a credit provided the vehicle you are planning to purchase also qualifies. There are different qualifications for new vehicles and previously owned (used) vehicles.

**New Vehicles -** The qualifications for new vehicles include the requirement they be assembled in North America, the vehicle's manufacturer's suggested retail price (MSRP) must be less than $80,000 for vans, pickups, and SUVs, and $55,000 for others, and must have a minimum battery capacity of 7 kilowatts or greater. In addition, for sales on or after April 18, 2023, a vehicle must meet certain critical mineral and battery component regulations. Those regulations require 40% of these components to be extracted or processed in the United States or in any country with which the United States has a free trade agreement, or recycled in North America. The percentage will increase until 2026 at which time the percentage will top out at 80%. The goal being to eliminate auto makers from reliance on certain foreign sources for these materials.

Luckily, the U.S. Department of Energy website provides an online tool to search for qualifying vehicles. It provides the amount of credit the vehicle may qualify for (maximum $7,500). Although it lists the MSRP cap for each vehicle, you as a buyer will need to verify the MSRP for the specific vehicle which can be lower or higher depending upon the upgrades or accessories included with the vehicle.

**Previously Owned Clean Vehicles** – The credit and vehicle qualifications are substantially different for previously owned clean vehicles. A previously owned clean vehicle is a motor vehicle that meets the following requirements:

- The model year is at least two years earlier than the calendar year in which the vehicle is acquired.
- Original use of the vehicle starts with a person other than the buyer,
- Is acquired in a qualified sale,
- Has a gross weight rating of less than 14,000 pounds,
- Is an eligible fuel cell vehicle or plug-in EV with a battery capacity of least 7 kilowatt hours, and
- Its use will be primarily in the United States.

Fortunately, the government provides an on-line index of qualifying previously owned vehicles that includes over 20 manufacturers and those included in the index satisfy the weight and battery capacity requirements.

*Qualified Sale for previously owned clean vehicle* - A qualified sale is:

- A purchase from a dealer (purchases from individuals do not qualify for the credit),
- Where the purchase price cannot be greater than $25,000,
- The first transfer of the vehicle since this credit was enacted and is to a qualified buyer other than the original buyer of the vehicle, and
- As mentioned earlier, the model year is at least two years earlier than the calendar year in which it is acquired. Thus for purchases in 2023, the model year must be 2021 or older.

*Qualified Buyer* - A qualified buyer is one that:

- Purchases the vehicle for use and not for resale,
- Is not a dependent of another taxpayer, and
- Has not been allowed a credit for a previously owned clean vehicle during the three-year period ending on the sale date.

*Credit Amount* - A qualified buyer who acquires and places in service a previously owned clean vehicle after 2022 and before 2032 is allowed an income tax credit equal to the lesser of:

- $4,000 or
- 30% of the vehicle's sale price.

**Dealer Report** – Whether you purchase a new or previously-owned clean vehicle, a dealer is required to supply both the buyer of the vehicle and the IRS a report that includes the buyer's name and taxpayer identification number (generally SSN), the vehicle's battery capacity, the vehicle identification number (VIN), maximum credit available, and in the case of a previously owned clean vehicle the purchase price.

This report serves two purposes, it provides the buyer with the information needed to claim a credit and prevents fraud by supplying the information to the IRS so they can verify legitimate credit claims. This information will be required to be included on the buyer's federal tax return for the purchase year for which the credit is claimed.

**What Tax Benefit Will These Credits Provide –** The clean vehicle credits are non-refundable and unused credit does not carry over to a subsequent year. Thus the credit will only offset your tax liability and any excess will be lost. So depending on your tax circumstances, even though you may qualify for the credit, you may not benefit from the full amount of the credit, and in some cases may not benefit from the credit at all. Accordingly, it may be appropriate to consult with this office in advance to determine what tax benefit a clean vehicle credit will provide you and avoid an unpleasant surprise at tax time.

**Credit Transfer to a Dealer** – You may have heard about the ability to transfer the credit in advance to the vehicle dealer and reduce your upfront costs. That option is not available until after 2023. Once available, you can, on or before the purchase date, elect to transfer the clean vehicle credit to the dealer from whom you are purchasing the vehicle in return for a reduction in purchase price equal to the credit amount. But be aware of a potential tax trap. If your MAGI for the current year and the preceding year exceeds the applicable MAGI limit, you will be required to recapture the amount of the advance credit on your tax return for the year the vehicle was purchased.

Understanding which vehicles qualify for these tax credits, whether you qualify for the credit and your potential tax benefits can be quite complicated and overwhelming. In addition, the IRS is still formulating and refining the rules and regulations about these credits. Call this office for assistance.

## Did You Get a Letter from the IRS? Don't Panic.

Since the IRS now does most of its auditing through correspondence, an IRS letter can likely increase your heart rate and, in some cases, even ruin your day, but don't panic.

When the IRS thinks it detects a potential issue with your tax return, it will contact you via U.S. mail; this is generally done with a CP-series notice. The IRS currently has over 150 varieties of CP notices. Please note that the IRS's first contact about a tax delinquency or discrepancy will never be a phone call or email. Such calls and emails are a common tool of scammers; if you get one, simply hang up the phone or delete the email. If you are concerned about the validity of a given message, please call this office.

Most commonly, CP notices describe the proposed tax due, as well as any interest or penalties. The notice will also explain the examination process and describe how you can respond.

As the IRS tries to close the tax revenue gap, it has become more aggressive in its collection efforts, so these notices which are sent out year-round, are becoming more common.

The first step the IRS uses in its review process involves matching what you reported on your tax return to the data that third parties (e.g., employers, banks, and brokers) reported. When this information does not agree, an automated collection effort begins.

**Don't Panic –** These CP notices often include errors. However, you do need to respond before the deadline specified on the notice (usually 30 days) or else face significant repercussions. The notice may even be related to suspected ID theft. For instance, someone may have gained access to your tax ID (or that of your spouse or one of your dependents) and tried to file a return using the stolen ID. The first step is to determine which type of notice you have received.

Sometimes, the IRS will be correct. You may have overlooked a capital gain or income from a second job. It is also possible that the IRS has caught someone else using your SSN in order to work or otherwise stealing your identity. Quite frequently, however, the IRS is incorrect, simply because its software isn't sophisticated enough to pick up all the information that you report on the schedules attached to your return.

These notices of proposed change will usually include penalties and interest. Even if you do owe the tax, this office may be able to get the penalties abated for due cause.

When you receive an IRS notice, your first step should be to **immediately contact this office** and to provide us with a copy of the notice. We will review the notice to determine whether it is correct, and then we will consult with you to determine how best to respond.

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The contents of this newsletter are intended to convey general information only and not to provide accounting or tax advice or opinions. The content should not be construed as, and should not be relied upon for, accounting or tax advice in any particular circumstance or fact situation. We recommend you contact us to discuss the application to any specific situation.

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