

SEMICONDUCTOR INDUSTRY INFORMATION MEMO

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Treasury Department Publishes Notice of Proposed Rule Making for the Advanced Manufacturing Investment Credit

On March 23, 2023 the U.S. Department of Treasury (Treasury) and the Internal Revenue Service (IRS) published the proposed rules for the implementation of the Advanced Manufacturing Investment Credit (Credit), also known as the 48D credit, established by the CHIPS Act of 2022. The publication of the long-awaited Treasury guidance coincides with the release of the Department of Commerce's Notice of Proposed Rulemaking detailing their plans for national security guardrails (Commerce Notice).

The proposed rules address the Credit's eligibility requirements, an election that eligible taxpayers may make to be treated as making a payment of tax, or for an eligible partnership or S corporation to receive an elective payment instead of claiming a credit, and a special 10-year credit recapture rule that is triggered by certain transactions.

Taxpayer Eligibility

A taxpayer is eligible for the Credit if they are not a foreign entity of concern and has not made an applicable transaction during the taxable year. For purposes of the Credit, a foreign entity of concern shares the same definition as provided in the Commerce Notice. An applicable transaction is any significant transaction involving the material expansion of semiconductor manufacturing capacity of the taxpayer in the People's Republic of China or a foreign country of concern.

Determination of Credit

The amount of the Credit for any taxable year for an eligible taxpayer is an amount equal to 25% of the taxpayer's basis in any qualified property which is part of an advanced manufacturing facility that is placed into service during such taxable year. The Credit is only available with respect to qualified property that the taxpayer places into service after Dec. 31, 2022, and for any qualified property on which construction began prior to Jan. 1, 2023. The amount of the Credit available for the latter is limited to the extent of the basis of that property that is attributable to the construction, reconstruction or erection of that property occurring after Aug. 9, 2022 (the date on which the CHIPS and Science Act was passed). Any portion of the basis that is attributable to qualified rehabilitation expenditures are excluded from the taxpayer's basis for the purposes of calculating the Credit amount. The Credit is not available to a taxpayer who places a qualified property in service in any year if construction did not begin on that property prior to Dec. 31, 2026.

The proposed rules contain special rules for passthrough entities such as partnerships, S corporations, and estates or trusts. In the case of a partnership, each partner must take into account separately the partner's share of the basis of the qualified property placed in service by the partnership during the taxable year. The basis of qualified property placed into service by an S corporation must be apportioned pro rata among the S corporation's shareholders as of the last day of the S corporation's taxable year.

In the case of an estate or trust, the basis must be apportioned among the estate or trust and its beneficiaries in proportion to the amount of income allocable to each.

Qualified Property

The term qualified property is defined as tangible depreciable property that is integral to the operation of an advanced manufacturing facility that is either (1) constructed, reconstructed or erected by the taxpayer, or (2) acquired by the taxpayer if the original use of such property commences with the taxpayer. Under the proposed rule tangible depreciable property does not include a building or its structural components, or a portion thereof, that is used for offices, administrative services such as HR or personnel services, payroll, legal and accounting services, and procurement services, sales or distribution functions, security services (not including cybersecurity), and any other functions not relating to manufacturing of semiconductors or semiconductor manufacturing equipment.

Under the proposed rule, property is deemed integral to the operation of an advanced manufacturing facility if the property is used directly in the manufacturing operation, is essential to the completeness of the manufacturing operation and is not transformed in any material way as a result of the manufacturing operation. The proposed rule also states that property is constructed, reconstructed or erected by the taxpayer if the work is done for the benefit of the taxpayer in accordance with the taxpayer's specifications. Lastly, the term original use is defined as the first use to which the property is put by any taxpayer in connection with a trade or business or for the production of income, with an exception for property initially held for sale in the ordinary course of business. Following the purchase of a piece of property initially held for sale in the ordinary course of business, the subsequent buyer would be considered the original user, and the original use would commence on the first day the buyer uses the property in a trade or business, or for the production of income.

Elective Payment Election

The proposed rule would allow a taxpayer to elect to have the credit be treated as making a payment of income tax, or for a partnership or S corporation to receive an actual payment in lieu of claiming the Credit. The election must be made by the due date of the taxpayer's income tax return for the year in which the election is going to be made (no earlier than May 8, 2023), and such election is irrevocable. The election for a partnership or S corporation that holds property that is eligible for the Credit must be made by the partnership or the corporation, not the shareholders.

If a taxpayer makes the elective payment election, and it is determined that the amount of the credit treated as a payment, or actually paid to the taxpayer exceeds what the taxpayer would have been eligible for had they not taken the election, the taxpayer will be liable for the amount in excess of what they were entitled to without taking the election, as well as a 20% penalty on that amount.

Credit Recapture

Under the proposed rules, a taxpayer forfeits eligibility for the Credit, and becomes liable for the entire amount of the Credit if the taxpayer partakes in an applicable transaction during the applicable period, which is 10 years beginning the date the taxpayer placed the property in service. An applicable transaction is defined as any significant transaction involving the material expansion of semiconductor manufacturing capacity of the taxpayer in any foreign country of concern. The proposed rule states that an increase in the aggregated manufacturing capacity during the applicable period greater than

5% constitutes a material expansion. A significant transaction includes any investment that is valued at \$100,000 or more.

A taxpayer may avoid forfeiture of eligibility if they can show that the applicable transaction has been ceased or abandoned within 45 days of a determination and notice by the Commissioner.

If you have any questions about the information presented in this memo, please contact [Robert Kirchner](#), [Jared Joyce](#), any attorney in Bond's [semiconductor industry group](#) or the Bond attorney with whom you are in regular contact.

