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The Inflation Reduction Act of 2022 was signed into law by President Biden on Aug. 16. Interestingly, this Act began its journey into becoming law under a completely different name and year. The Act was originally introduced to the House of Representatives in September 2021 as the Build Back Better bill.

By: Dr. Michelle Freeman, CPA

The original bill was poised to increase the $10,000 state and local tax deduction cap, increase the Child Tax Credit, extend the changes to the Earned Income Tax Credit and increase taxes on high-income individuals (Nevius, 2022). Accountants and taxpayers, surmising that it would affect the nearing tax season with several changes, anxiously awaited its passing as 2021 came to an end; however, none of the items above survived the deliberations or the year-end deadline. In 2022, the bill took on a new focus to reduce inflation and became the Inflation Reduction Act of 2022. The final vote was narrow, with Vice President Harris casting the tie-breaking vote for a 51-50 outcome. The Act attempts to reduce inflation by accomplishing four main tasks: deficit reduction, prescription drug price reduction, domestic energy investment and clean energy promotion. There are mixed reviews on whether the bill will actually reduce inflation or whether it could possibly increase it.

The Inflation Reduction Act is packed with items other than tax provisions; however, there are a few notable tax provisions. The larger tax implications of the Act include the following:

- Corporate Alternative Minimum Tax (AMT)
- Excise tax on corporate stock repurchases
- IRS funding
- Excise tax on drug manufacturers for non-compliance
- Affordable Care Act Premium Tax Credit extension
- Clean energy tax credits for individuals and businesses

The first three listed above deal with the deficit reduction agenda in the bill. Below, we will summarize some of the highlights of these provisions.

Corporate Alternative Minimum Tax (AMT)

Corporate AMT, repealed with the Tax Cuts and Jobs Act in 2017, returns with a fresh look and calculation in the Inflation Reduction Act. The resurgence of the corporate AMT is the largest of the revenue raisers based on tax provisions. In an interview conducted by Neil Amato, writer for the Journal of Accountancy, with Adam Schrom, CPA, director of product management at Bloomberg Tax, Schrom stated that he believed that Congress brought back the AMT due to the "perceived inequity with the current system" (Amato, 2022). He stated that there are "a lot of companies reporting significant accounting profits to their shareholders while paying little to nothing in U.S. tax" (Amato, 2022).

The Act imposes a 15% AMT on the corporation's "adjusted financial statement income for the year … over the corporate AMT foreign tax credit for the taxable year" (H.R. 5376 Sec. 10101 (a)(2)(A)). Noteworthy is that the starting point for the calculation is book income, not taxable income as it had always been prior to TCJA. It is then adjusted for a laundry list of items, such as depreciation differences between book and tax income.

The corporate AMT will be imposed upon a corporation (other than S corporations, regulated investment companies or real estate investment trusts) "which meets the average annual adjusted financial statement income test for one or more taxable years" beginning after Dec. 31, 2022 (H.R. 5376 10101(a)(2)). The average annual adjusted financial statement income test averages three years of income. If that amount is more than $1 billion, then they are subject to the AMT, with some exceptions.

Corporations that are members of a foreign parented multinational group are also subject to the AMT imposition if the three-year average of combined annual adjusted financial statement income of all members of the group is $1 billion and the member has average annual adjusted financial statement income of $100 million or more (H.R. 5376 Sec. 10101 (a)(2)). Once a corporation meets the AMT requirement, they retain this status unless they meet further exceptions (H.R. 5376 Sec. 10101(a)(2)).

According to Thomson Reuters, "the Joint Committee on Taxation, Proposed Book Minimum Tax analysis, July 28, 2022, estimates that about 150 taxpayers would be subject to the corporate minimum tax annually," approximately "30% of existing Fortune 500 companies," which is "an incredibly narrow base making 150 companies responsible for raising $313 billion of the anticipated $450 billion required to cover go-green decarbonization expenditures in the Act" (Thomson Reuters, 2022).

Excise Tax on Corporate Stock Repurchases

The Act imposes a 1% tax on the difference between the FV of corporate stock repurchased by the corporation and the FMV of new stock issued by the corporation during the tax year, including stock issued to employees. Stock repurchases where the total FMV is less than or equal to $1 million are exempt. The excise tax begins after Dec. 31, 2022 (H.R. 5376 Sec. 10201(a)). Schrom explains that stock buybacks exploit "the perceived loophole in the system," which is the difference in tax on a non-qualified dividend taxed at ordinary rates and a stock buyback taxed at capital gains rates to only those who choose to sell (Amato, 2022). He believes that the policy intends to "theoretically equalize the tax treatment of dividend and buybacks so at least tax considerations don't determine the decision to either buy back stock or pay a dividend" (Amato, 2022). However, at only a 1% rate, he does not think it will have much impact (Amato, 2022).

Funding the IRS and Improving Taxpayer Compliance

The additional funding to the IRS is estimated to raise $204 billion through 2031 in revenue (Nevius, 2022). This additional funding will cost the Act approximately $80 billion, split as follows:

- Taxpayer services, including pre-filing assistance and education, filing and account services, and taxpayer advocacy services at a cost of $3.18 billion (H.R. 5376 10301(1)(A)(i)).
- Enforcement, including activities to "determine and collect owed taxes, to provide legal and litigation support, to conduct criminal investigations," and other services at a cost of $45.6 billion (H.R. 5376 10301(1)(A)(ii)).
- Operations "to support taxpayer services and enforcement programs, including rent payments; facilities; … the operations of the Internal Revenue Service oversight board; and other services" at a cost of $25.3 billion (H.R. 5376 10301(1)(A)(iii)).
- Business systems modernization, including "development of callback technology … to provide a more personalized customer service" at a cost of $4.75 billion (H.R. 5376 10301(1)(A)(iv)).

Some argue that the IRS' increased funding will be aimed at the middle class and small business; however, Secretary Yellen sent a letter to IRS Commissioner Rettig "specifically directing that the new funding not be used to increase audits on taxpayers earning less than $400,000 annually" (Amato, 2022).

Excise Tax on Drug Manufacturers for Noncompliance

The Act requires Medicare and Medicaid to negotiate prices of certain prescription drugs that do not have other generic choices available. Drug manufacturers who are in noncompliance will pay an excise tax during the noncompliance period (H.R. 5376 Sec. 11003).

Affordable Care Act Premium Tax Credit

The ACA premium tax credit is extended through 2025 to taxpayers whose income exceeds 400% of the poverty line (H.R. 5376 Sec. 12001(b)).

Clean Energy Tax Credits for Individuals and Businesses

Clean energy is a heavy focus of the Act, and there are several new clean energy tax credits as well as modifications and extensions of others. Several of the credits have requirements such as "prevailing wages, apprenticeship programs, domestic content, and distressed communities," which "complicate the ability to qualify for the maximum credits but are designed to promote other societal goals" (Luscombe, 2022). Below are summaries of some of the most notable ones:

Energy-efficient Home Improvement Credit (previously the Nonbusiness Energy Property Credit) is extended through 2032 and is increased from 10% to 30%. It replaces a $500 lifetime cap with $1,200 per year. It includes expenditures for energy-efficient improvements installed or paid during the year, and it now also includes a 30% credit for expenditures for home energy audits (H.R. 5376 Sec. 13301).

Residential Clean Energy Credit (previously the Residential Energy-efficient Property Credit) is extended through 2034 and now adds qualified battery storage technology expenditures to the eligible list of expenditures (H.R. 5376 Sec. 13302).

Energy-efficient Commercial Building Tax Deduction contains new requirements that take effect in 2023 and higher deduction limits (H.R. 5376 Sec. 13303).

Energy-efficient Home Tax Credit is extended through 2032. It increases the credit to $2,500 if a new home meets Energy Star efficiency standards and $5,000 for new homes that are certified as zero-energy ready homes. Credits are also available for energy-efficient multifamily dwellings (H.R. 5376 Sec. 13304).

Clean Vehicle Credit (formerly known as the credit for electric vehicles) now has multiple requirements, including:

- final assembly of the vehicle must occur in North America,
- 40% (80% after 2026) of "critical minerals used in the car must have been extracted or processed in the United States or in a country with which the U.S. has a free trade agreement,"
- 50% (100% after 2026) of the battery components must be manufactured in the United States.

It is allowed only one time per vehicle, but the cap on the quantity of vehicles is removed. There is also a MAGI limit and a price cap on the vehicle. Cars must cost less than $55,000, while vans, SUVs or pickup trucks must cost less than $80,000. The new credit applies to vehicles purchased after Dec. 31, 2022, and extends to 2032 (Section 13401).

Used Clean Vehicle Credit is a new credit up to $4,000. A MAGI limit is applied, and the sales price of the vehicle must be $25,000 or less (Section 13402).

Qualified Commercial Clean Vehicle Credit is a new credit equal to the lesser of 15% of the basis of the vehicle or the "incremental cost" (difference between the cost of the commercial clean vehicle and the cost of a comparable gasoline or diesel-powered vehicle). The credit is capped at $7,500 for vehicles less than 14,000 pounds and $40,000 for all other vehicles (Section 13403).

Alternative Fuel Refueling Property Credit is extended, but in 2023 it adds a requirement that it can only be applied to property "located in a rural or low-income census tract" in an attempt to accomplish other social and economic goals (Luscombe, 2022), (Section 13404).

Other Provisions

The Act contains a few other tax provisions, including:

- An increased $250,000 allowance for research credits to offset against payroll tax for small businesses (H.R. 5376 Sec. 13902)
- The extension of the limit on excess business losses of noncorporate taxpayers through 2028 (H.R. 5376 Sec. 13903)
- The finalization of the permanency of the coal tax to fund the Black Lung Disability Trust Fund (H.R. 5376 Sec. 13901)

Conclusion

The Act seems to have accomplished many of the Democratic agenda items for health care and clean energy. It did not, however, provide much tax relief for lower- and middle-income taxpayers, who may be shocked in April when their tax refunds are diminished due to the loss of the previous expansion of the Child Tax Credit and Earned Income Tax Credit.

About the Author

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