The Inflation Reduction Act (IRA) of 2022

September 22, 2022

Ong & Company
certified public accountants

Agenda

- What is the Inflation Reduction Act?
- What are the highlights?
- What proposals were not included?
- What are the numbers?
- What are the details?
- What are the key takeaways and recommended next steps?

What is the Inflation Reduction Act?

The Inflation Reduction Act (IRA) of 2022 is the significantly slimmed down version of President Biden's Build Back Better Plan

- January 20, 2021: Inauguration of Joe Biden
- April 28, 2021: Biden administration releases Build Back Better Plan
- July 13, 2021: Budget Committee Democrats and White House agree on $3.5T budget reconciliation package
- July - December 2021: Senators Manchin (D-WV) and Sinema (D-AZ) raise objections to the $3.5T
- December 2021: Trimmed down Build Back Better Plan of $1.75T dies in Senate due to opposition from Manchin
- July 27, 2022: Senate Majority Leader Schumer and Manchin announce agreement on Inflation Reduction Act
- August 16, 2022: President Biden signs IRA into law after passed by congress with sole support from Democrats

What are the highlights of the IRA?

Clean Energy & Climate Change

- Massive Expansion and Extension of Clean Energy Tax Credits and Incentives
- Additional Excise Taxes on Fossil Fuels

Corporate Taxes

- New 15% Corporate Alternative Minimum Tax (AMT) on Financial Statement Income
- New 1% Excise Tax on Stock Buybacks

Individual & Small Business Taxes

- Additional $80B in IRS Funding for Enforcement and Administration
- 2-Year Extension of Passthrough Loss Limitations
- Increase in Research & Development Tax Credit that can be Applied Against Payroll Taxes

Health Care

- Extension of Affordable Care Act Premium Tax Credits through 2025
- Prescription Drug Pricing Reform

What proposals were not included in the IRA?

- Increase to Corporate Tax Rate
- Increase to Individual Tax Rates
- Expansion of Net Investment Income Tax
- Elimination of Basis Step-up at Death
- Increase to / Expansion of Capital Gains Taxes
- Implementation of Wealth Surtaxes
- Expansion of the Child Tax Credit
- Expansion of the Dependent Care Credit
- Expansion of the Earned Income Tax Credit
- Restoration of the State & Local Tax (SALT) Deduction (limit $10,000 scheduled to expire after 2025)
- Carried Interest Tax Reform (proposed increase of holding period from 3 to 5 years)
- INFLATION REDUCTION

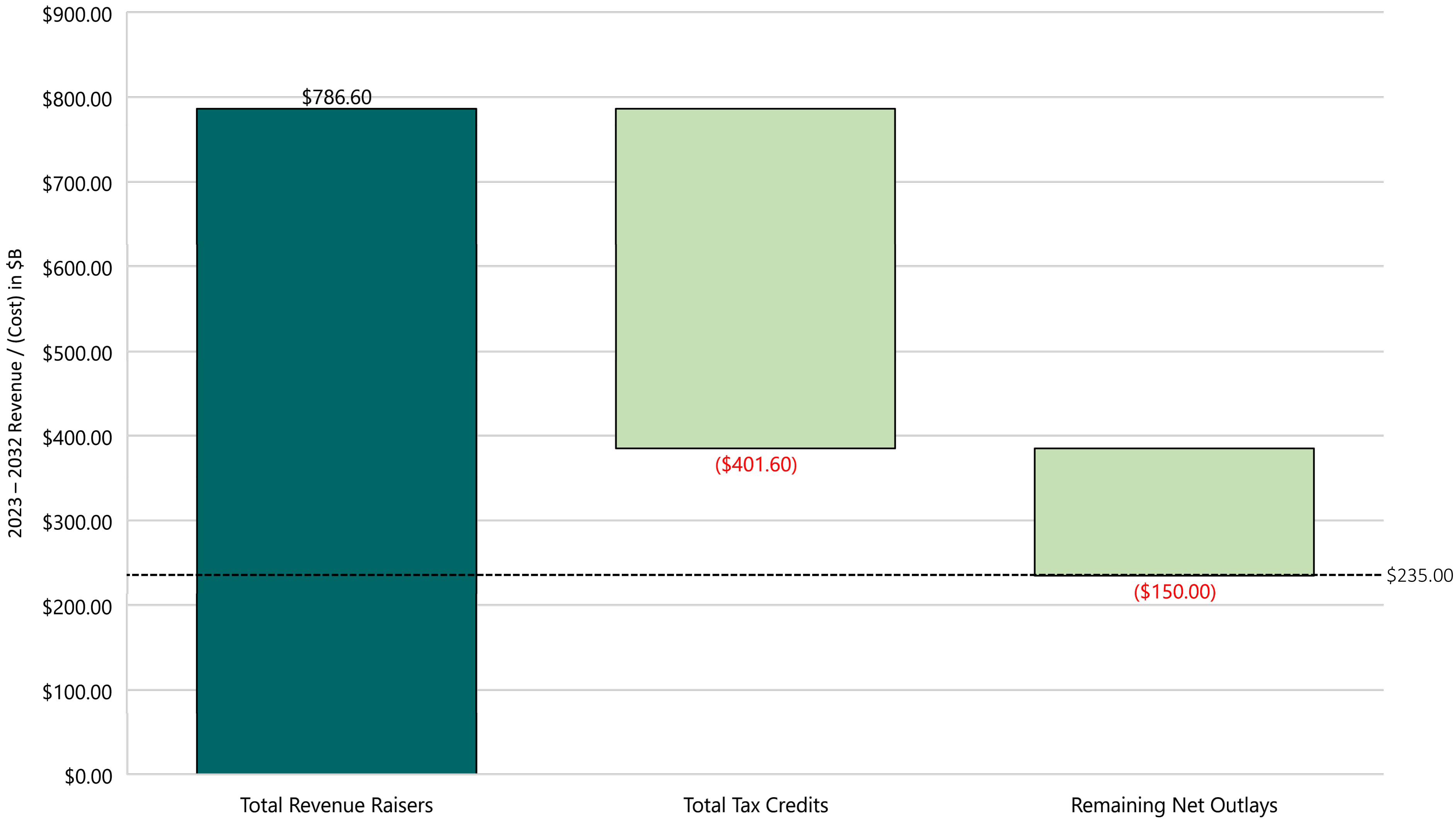
What are the numbers?

Provision (Billions of Dollars)	2023-2032
Individual Provisions	
Extend the limitation on passthrough business excess losses for two years	$53.90
Corporate Provisions	
Impose a 15% minimum tax on corporate book income for corporations with profits over $1 billion	$182.50
Levy a 1% excise tax on stock buybacks	$54.90
Raises taxes in the federal superfund program	$13.70
Items Scored by Joint Committee on Taxation	
Other unscored tax provisions	$1.20
Other Revenue Raisers	
Spend an additional $80 billion in IRS enforcement (net revenue)	$151.50
Impose drug pricing provisions	$329.00
Total Revenue Raisers	$786.60
Scored Tax Credits	
Provide tax credits for green energy	($332.00)
Extend expanded Affordable Care Act healthcare subsidies through 2025	($69.60)
Total Tax Credits	($401.60)
Total Conventional Revenue	$385.00
Total Dynamic Revenue	$361.10
Remaining Net Outlays	($150.00)
Conventional Deficit Impact (before interest costs)	$235.00
Dynamic Deficit Impact (before interest costs)	$211.10

Source: Tax Foundation General Equilibrium Model, August 2022. Items may not sum due to rounding.

Note: "Remaining Net Outlays" include estimated spending on energy and health provisions scored by the Congressional Budget Office and adjusted for $5 billion in drought resilience funding added by the Senate.

What are the numbers?



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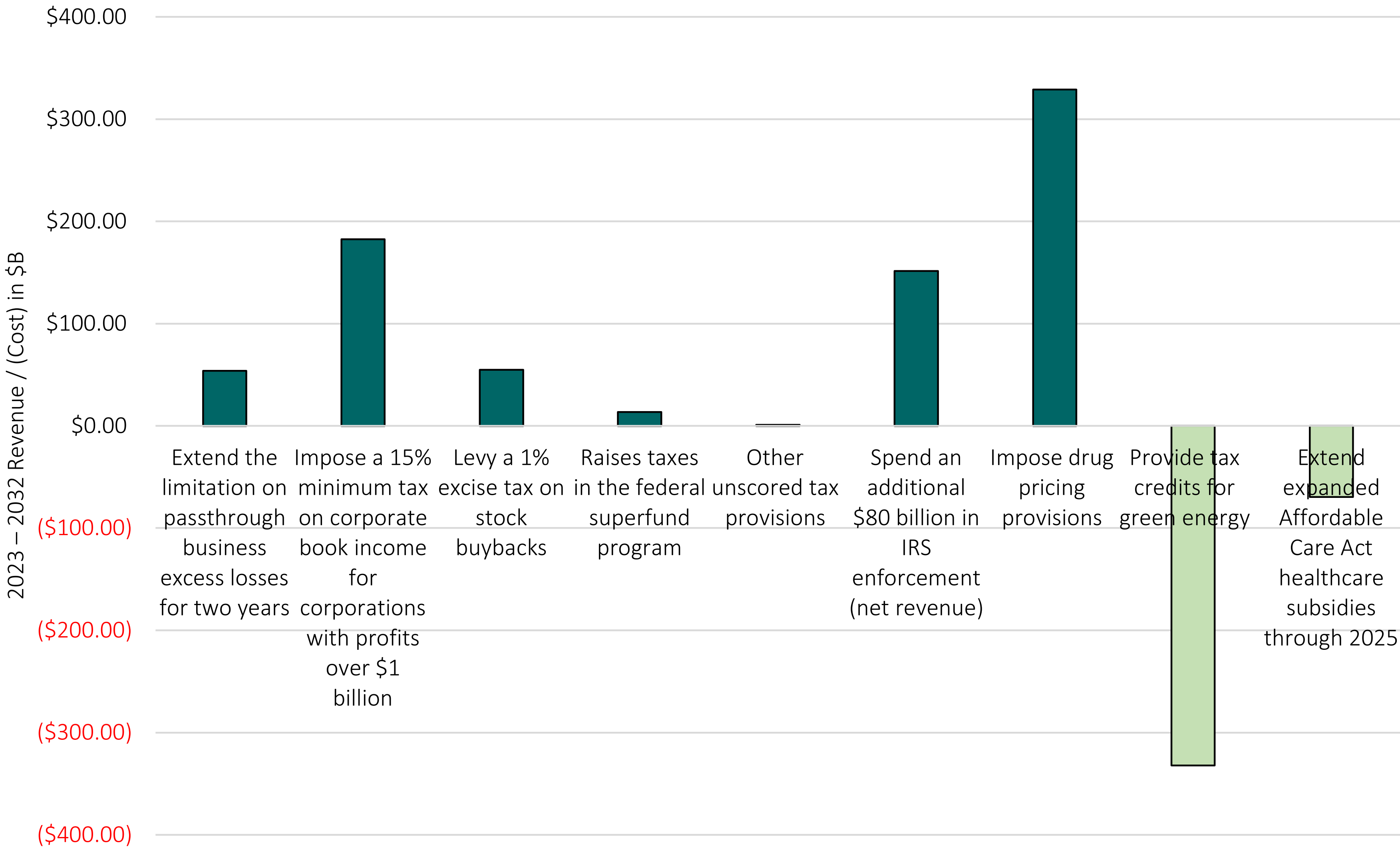

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Clean Energy & Climate Change

Massive Expansion and Extension of Clean Energy Tax Credits and Incentives

Clean Vehicle Credit

- Replaces the prior Electric Vehicle Credit as of August 16, 2022
- Includes both plug-in electric vehicles and fuel cell vehicles
- Eliminates the limitation on the number of vehicles produced by a specific manufacturer
- Requires final assembly of the vehicle in North America with phase-in of sourcing requirements for critical components over time
- Credit can be directly applied at the time of the purchase by dealership transfer beginning in 2024

New Clean Vehicles

- The maximum credit amount for new vehicles remains at $7,500
- MSRP cannot exceed $55,000 for sedans and $80,000 for SUVs, trucks, and vans
- Income limitation of $150,000 for Single, $225,000 for Head of Household, and $300,000 for Married Filing Jointly (prior year or year of purchase MAGI)

Used Clean Vehicles

- New credit of lessor of $4,000 or 30% of purchase price is available for the purchase of used clean vehicles
- Income limitation of $75,000 for Single, $112,500 for Head of Household, and $150,000 for Married Filing Jointly (prior year or year of purchase MAGI)

Qualified Commercial Clean Vehicles

- New credit of up to $7,500 for vehicles with a GVWR of less than 14,000 pounds and up to $40,000 for heavier vehicles
- Credit is lesser of 15% of the vehicle's basis (30% for vehicles not powered by gas or diesel engine) or the incremental cost of the clean vehicle over the cost of a comparable vehicle powered by gas or diesel only

Buyer Requirements for Clean Vehicle Credits

- Purchases must not be for resale
- Buyer cannot be a dependent of another taxpayer
- Buyer must not have claimed a clean vehicle credit during the 3-year period ending on the date of purchase

Massive Expansion and Extension of Clean Energy Tax Credits and Incentives

- Residential Energy Incentives
  1. Nonbusiness Energy Property Credit – now Energy-Efficient Home Improvement Credit
     - Extends and enhances the Nonbusiness Energy Property Credit, which previously expired at the end of 2021
     - Credit is 30% (previously 10%) and applies to energy-efficient windows, doors, insulation, skylights, and HVAC
     - The previous lifetime limit on the credit of $500 is replaced with an annual limit of $1,200 (the annual cap is $2,000 for heat pumps, water heaters, and boilers) beginning in 2023 and running through 2033
  2. Residential Clean Energy Credit
     - The Residential Clean Energy Credit is also a 30% credit and applies to installation of solar panels or other equipment that harnesses renewable energy (wind, geothermal, biomass fuel)
     - The Residential Clean Energy Credit is retroactive back to beginning of 2022, and the 30% credit runs through 2032 (reduced credit of 26% in 2033 and 22% in 2034)
     - Credits apply in the year the project is finished and placed into service

Planning Note: The clean vehicle credit and residential energy credits are nonrefundable, so plan accordingly to make sure you time the credits in a year that you have total tax to absorb the credit. Consider timing the clean vehicle credit in or after low-income years for eligibility.

Massive Expansion and Extension of Clean Energy Tax Credits and Incentives

- Energy Provisions for Businesses
  1. New Energy Efficient Home Credit (for eligible contractors)
     - Previous credit existed since 2006 and most recently expired at the end of 2021
     - New credit retroactively extends the existing credit through 2022 and modifies it starting in 2023 for new energy-efficient homes sold through 2032
     - Credit is increased to $500, $1,000, $2,500, or $5,000 depending on which requirements the home satisfies
  2. Energy Efficient Commercial Buildings Deduction
     - 179D allows for accelerated depreciation deductions for energy-efficient commercial buildings
     - The IRA allows designers of buildings for tax-exempt organizations to claim the deduction
     - Previous allowance in effect through 2022 of $0.63 - $1.88 multiplied by the square footage of the building
     - New allowance beginning in 2023 is $1.00 - $5.00 multiplied by the square footage of the building with bonus deductions available

Planning Note: Certain clean energy credits can be issued as direct payments and/or can be transferable. A penalty will apply if taxpayer receives a larger direct payment than the credit to which it is entitled based on tax return.

Massive Expansion and Extension of Clean Energy Tax Credits and Incentives

- Clean Energy Manufacturing & Production Credits
  1. Clean Energy Production Credit
     - Extends the credit for production of electricity from renewable resources through 2024 at 1.5 cents per kilowatt hour
     - Increased credit available if entity meets workforce and wage requirements in operation of the facility
  2. Clean Energy Investment Credit & Advanced Energy Project Credit
     - Credit of up to 30% for the qualified investment in an eligible property which re-quips, expands, or establishes a manufacturing facility for the production, transfer, or storage of clean energy
     - Extended through 2024 with workforce / wage credit enhancements available
     - Adds energy storage technology, qualified biogas property, and microgrid controllers to qualifying types of property
     - Increased credit available for facilities place in service in connection with low-income communities
  3. Zero-Emission Nuclear Power Facility
     - Credit of 0.3 cents per kilowatt-hour for energy produced after 2023 and before 2033
  4. Clean Hydrogen Production
     - Credit available for the first 10 years that qualified clean hydrogen production facility is in service
  5. Credit for Sustainable Aviation Fuel
     - Sustainable aviation fuel credit of $1.25 per gallon of "qualified mixture," plus, where the greenhouse gas emissions reduction percentage for the qualified mixture exceeds 50%, an increase resulting in a credit of up to $1.75 per gallon

Planning Note: Several other industry-specific clean energy credits and incentives are available

Additional Excise Taxes on Fossil Fuels

- Hazardous Superfund Tax
  - Crude oil received at a US refinery and petroleum products entered into the US for consumption, use, or warehousing are subject to a 9 cents per barrel environmental excise tax, which funds the Oil Spill Liability Trust Fund
  - For tax years 2023 – 2025, these products are subject to both:
    - 9 cents per barrel Oil Spill Liability tax
    - 16.4 cents per barrel tax
  - After 2025, such crude oil and petroleum products are subject to only the inflation-adjusted Hazardous Substance Superfund tax
- Coal Excise Tax Rates Permanently Added
  - Coal excise tax rates apply at $1.10 per ton for coal from underground mines and 55¢ per ton for surface mined coal, not to exceed 4.4% of sales price
  - Prior to the IRA, producers paid reduced rates to fund the Black Lung Disability Trust Fund: 50¢ per ton for coal and 25¢ per ton for coal from surface mines, not to exceed 2% of the sales price

Corporate Taxes

New 15% Corporate Alternative Minimum Tax (AMT) on Financial Statement Income

- 15% AMT on corporations with average adjusted financial statement income (AFSI) that exceeds $1B over 3-year period ending with year prior to current tax year (2020-2022 for 2023)
- AMT will be applied on adjusted financial statement income (AFSI)
- Adjusted financial statement income is equal to book income with specific adjustments, including accelerated tax depreciation on fixed assets
- Corporations will need to calculate new AFSI figure for three prior years
- The income threshold for AMT is lower if part of a foreign multinational group
    - If foreign multinational exceeds $1B threshold, then then AMT applies if the 3-year average AFSI of US subsidiaries exceeds $100M
- Effective for tax years beginning after December 31, 2022
- Estimated to impact 150 total corporations

Planning Note: Corporate AMT was applicable prior to elimination with the TCJA in 2018, but it was previously based on taxable income as determined by the IRS. The concept of using financial statement income (determined by the Financial Accounting Standards Board) is new.

New 1% Excise Tax on Stock Buybacks

- Imposes an excise tax on publicly traded corporations that repurchase their stock
- Tax is equal to 1% of the fair market value of the repurchased stock
- The tax paid is not deductible to the corporation
- Effective for repurchases that occur after December 31, 2022
- Treasury department can apply the excise tax to any economically similar transaction to buyback
- There are several exceptions where the tax would not apply, including the following scenarios:
  1. Total value of stock repurchased does not exceed $1M during the taxable year
  2. Transaction is part of a Section 368(a) reorganization
  3. Stock is contributed to an employer-sponsored retirement plan
  4. Repurchase is by a dealer in securities as part of ordinary business
  5. Repurchase is made by a Regulated Investment Company (RIC) or a Real Estate Investment Trust (REIT)
  6. Repurchase is treated as a dividend

Planning Note: Stock buybacks are more tax efficient than dividends for investors. Monitor investment accounts for larger dividend payments and associated tax impact rather than unrealized capital gains associated with stock price increases from buybacks.

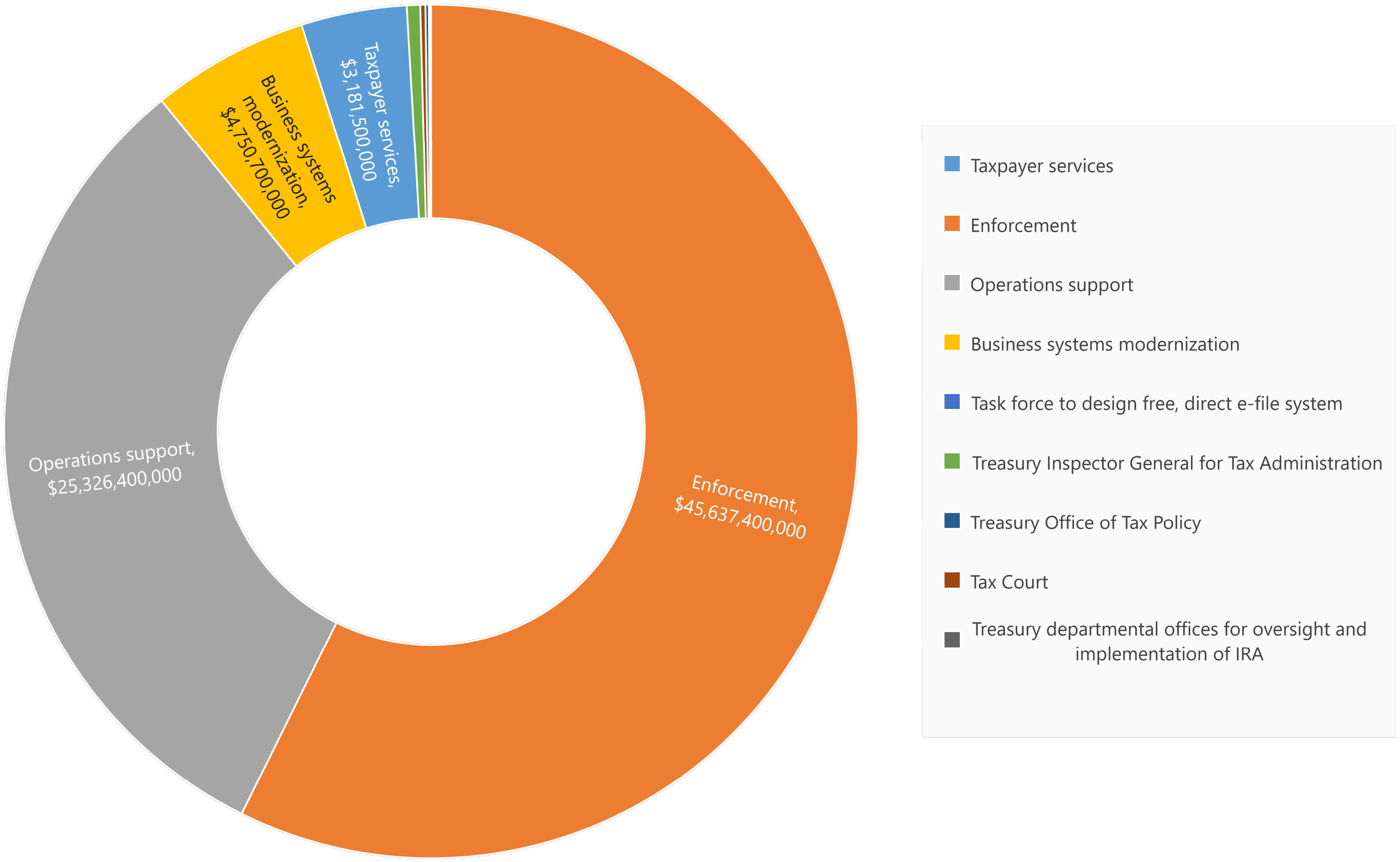
Individual & Small Business Taxes

Additional $80B in IRS Funding for Enforcement and Administration

- Focus of the $80B is to close the tax gap by allocating an increased amount to the IRS to improve enforcement
- Increased collections of $231.5B projected over time period of 2023 -2032 (net of $151.5B)
- $45.6B of the total will be allocated to enforcement efforts
- IRS had total expenditures of $13.7B in FY 2021 (including supplemental funding for COVID-19 expenses)
- ~87,000 of new IRS staffers will replace more than 50,000 set to retire over next 10 years
- Includes greater flexibility for the IRS to direct hire candidates
- Expect increase in audit rates for high-income earners, more automated matching, more automated letter audits, and greater focus on digital currency and foreign transaction compliance

Planning Note: Treasury Secretary Janet Yellen issued a directive that the IRS should implement new programs in such a way as to not increase examination rates of taxpayers making less than $400,000

Additional $80B in IRS Funding for Enforcement and Administration



2-Year Extension of Passthrough Loss Limitations

Last-Minute Addition

- Extends the limitation on the deductibility of excess business losses applied from passthrough entities (Partnerships, S-Corporations) for an additional 2 years, through 2028
- Passthrough business losses are limited to $270,000 for Single and Head of Household, and $540,000 for Married Filing Jointly (amounts adjusted for inflation annually)
- Excess losses can be carried forward to the next taxable year
- This was originally enacted as part of the Tax Cuts & Jobs Act of 2017 and was scheduled to be effective for tax years 2018 – 2025
- The Coronavirus Aid, Relief, and Economic Security (CARES) Act of 2020 retroactively delayed the implementation to the 2021 tax year
- The American Rescue Plan Act (ARPA) of 2021 extended this for 1 year, through 2026
- This was thrown in as a last-minute addition as a revenue raiser to replace closing the "carried interest loophole" that was opposed by Krysten Sinema (D-AZ)

Planning Note: Republicans had planned to use an extension of this limitation to fund an extension of the 20% qualified business income (QBI) deduction. This being included in the IRA creates a larger hurdle to extend the QBI deductions beyond the 2025 scheduled expiration

Increase in Research & Development Tax Credit that can be Applied Against Payroll Taxes

- Qualified small businesses have been allowed to claim a credit associated with Research & Development expenses of up to $250,000 against payroll taxes since 2015
- The IRA increases this limit to $500,000 beginning in 2023

Planning Note: Claiming the R&D credit against payroll taxes can be a great option for small businesses that are generating a loss in early years of operation

Health Care

Extension of Affordable Care Act Premium Tax Credits through 2025

- The IRA extends the ACA provisions from the American Rescue Plan Act of 2021 that were set to expire at the end of 2022
- For 2021 and 2022, the ARPA increased the credit amount for eligible taxpayers by reducing the percentage of annual household income they're required to contribute toward their health insurance premium
- Extends the temporary exception to the 400% of federal poverty line cap through the 2025 tax year
- Permits people with household incomes over that amount three more years to claim the premium tax credit
- Estimated 1.1M Americans eligible for the 2022 credit that would not have qualified if the 400% cap had not been lifted

Prescription Drug Pricing Reform

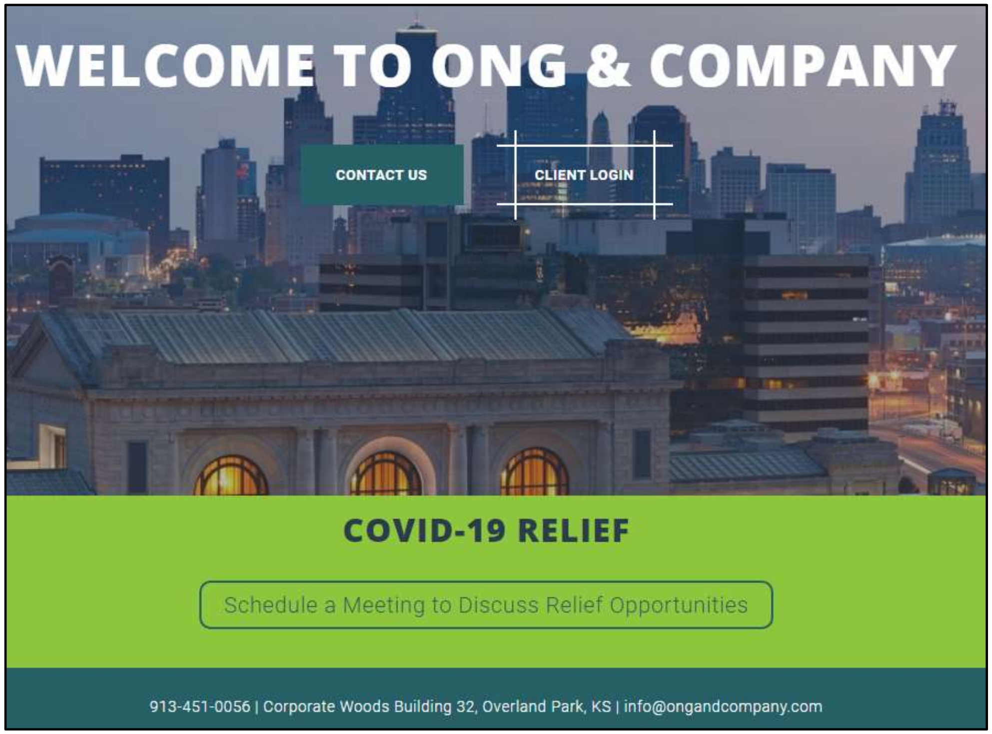
- Provisions Designed to Reduce Drug Prices
  - Requires the federal government to negotiate prices for some high-cost drugs covered under Medicare (previously prohibited under Medicare Modernization Act of 2003 – pharmaceutical industry has argued that allowing government to negotiate prices would stifle innovation)
  - Requires drug manufacturers to pay rebates to Medicare if they increase prices faster than inflation for drugs used by Medicare beneficiaries
- Provisions Designed to Reduce Out-of-Pocket Spending for Medicare Beneficiaries
  - Caps Medicare beneficiaries' out-of-pocket spending under the Medicare Part D benefit, first by eliminating coinsurance above the catastrophic threshold in 2024 and then by adding a $2,000 cap on spending in 2025
  - Limits cost sharing for insulin to $35 per month for people with Medicare, beginning in 2023
  - Eliminates cost sharing for adult vaccines covered under Medicare Part D, as of 2023, and improves access to adult vaccines under Medicaid and CHIP
  - Expands eligibility for full Part D Low-Income Subsidies (LIS) in 2024
- Delays implementation of the drug rebate rule until 2032, rather than take effect in 2027.
  - The rebate rule would eliminate the anti-kickback safe harbor protections for prescription drug rebates negotiated between drug manufacturers and pharmacy benefit managers or health plan sponsors in Medicare Part D
  - This rule was estimated to increase Medicare spending and premiums paid by beneficiaries

What are the key takeaways and recommended next steps?

- Almost all revenue-generating provisions of prior proposals have been eliminated from this bill, with only the corporate AMT, excise tax on stock buybacks, and increased funding for the IRS having survived from prior versions
- Keep an eye out for the sunset of TCJA provisions after 2025
    - Increase in Tax Rates
    - Reduction in Standard Deduction
    - Elimination of QBI Deduction
    - Elimination of SALT cap
- Monitor other provisions that were proposed but removed from IRA
- Monitor financial markets and investments for responses to corporate provisions
- Plan residential energy-efficient improvements carefully to optimize credits
- Confirm eligibility for other energy credits as opportunities are available

We’re here to help

Visit our website or click https://calendly.com/ongandcompany to select an available time for a virtual meeting with our team to discuss these updates and how they apply to your situation.



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Connect with us to learn more

If you have questions, be sure to reach out to our office. Our team is here to help!

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