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## TAX ALERT – SEPTEMBER 30, 2022

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### Key Tax Related Provisions of Inflation Reduction Act of 2022

#### **Introduction**

On August 16, 2022, President Biden signed into law the Inflation Reduction Act of 2022 (the “Act”). The Act addresses climate change, health care, inflation, and taxes. It is a significantly slimmed-down version of the Build Back Better Act, which passed the House of Representatives but failed to pass the Senate. The tax related provisions are more targeted than those that were proposed, and the revenue raisers affect, in particular, the largest corporations.

#### **15% Corporate Minimum Tax**

The Act imposes a 15% Alternative Minimum Tax (“AMT”) on the Adjusted Financial Statement Income (“AFSI”) of corporations with average annual AFSI in excess of \$1 billion, calculated over a three-year period. Financial statement income is adjusted, inter alia, by using tax and not book depreciation. According to the Joint Committee on Taxation, the tax would likely apply only to around 150 of the world’s largest companies. The tax is imposed to the extent the AMT exceeds the company’s regular tax including the base erosion and anti-abuse tax.

A United States (“US”) corporate subsidiary of a foreign-parented group will be subject to the AMT if the entire group meets the \$1 billion income threshold, and the subsidiary has an AFSI of \$100 million or more.

Corporations generally would be eligible to claim net operating losses and tax credits against the AMT and would be eligible to claim a tax credit against the regular corporate tax for AMT paid in prior years, to the extent the regular tax liability in any year exceeds 15% of the corporation’s AFSI.

This provision is effective for tax years beginning after December 31, 2022.

#### **Excise Tax on Stock Buybacks**

The Act imposes an excise tax on domestic publicly traded corporations that repurchase their stock directly (or through a more than 50% owned subsidiary corporation or partnership). The tax is equal to 1% of the fair market value of the repurchased stock and is not deductible.

The excise tax also would apply to repurchases of stock of publicly traded non-U.S. corporations by certain U.S. affiliates (in which case the U.S. affiliate would be liable for the excise tax) and repurchases of stock by publicly traded non-U.S. corporations that are classified as surrogate foreign

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corporations under Internal Revenue Code (“IRC”) §7874 (generally, a non-U.S. corporation that replaces the U.S. parent corporation of a multinational group in an inversion transaction).

The Act also provides certain exceptions. For example, the tax does not apply to the extent that: (i) the repurchase is part of a reorganization where no gain or loss is recognized by the shareholder; (ii) the repurchased stock (or an amount of stock equal to the value of the stock repurchased) is contributed to an employer-sponsored retirement plan, employee stock ownership plan or similar plan; (iii) the total value of stock repurchased during the taxable year does not exceed \$1 million; (iv) under regulations to be issued, the repurchase is by a dealer in securities in the ordinary course of business; (v) the repurchase is made by a RIC or a REIT, or (vi) the repurchase is treated as a dividend.

The provision is effective for repurchases that occur after December 31, 2022.

### **Extension of Limitation on Deductibility of Excess Business Losses**

The Act extends the limitation on the deductibility of excess business losses by non-corporate taxpayers under IRC §461(l) for another two years. This limitation was originally part of the Tax Cuts and Jobs Act in 2017 and restricts the extent a noncorporate taxpayer can use trade or business losses to offset other income. For 2022, the limitation for a married couple filing jointly adjusted for inflation is approximately \$524,000. Thus, any losses above this threshold are suspended and carried forward.

Before the Act, the limitation was set to expire in 2026; however, now it will apply for another two years through 2028.

### **Small Business Payroll Tax Credits for Research Activities**

Previously, qualified small businesses that incurred research expenses could elect to claim up to \$250,000 of a tax credit for increasing research activities as a payroll tax credit against the employer’s share of social security tax. A qualified small business is one that, in any given tax year, has gross receipts of less than \$5 million and did not have gross receipts for any tax year preceding the five-year tax period ending with the current tax year.

Under the Act qualified small businesses may apply an additional \$250,000 in qualifying research expenses as a payroll tax credit against the employer’s share of Medicare. The credit cannot exceed the tax imposed for any calendar quarter, and unused amounts of credit can be carried forward.

The provision is effective for tax years beginning after December 31, 2022.

### **Clean Energy Tax Credits**

The Act extends and expands existing energy-related tax credits and adds several new tax credits related to clean electricity, manufacturing, fuel, and vehicles. Through these enhanced energy tax

credits, approximately \$374 billion will be spent on climate and energy spending in what is being referred to as the largest investment in clean energy in US history.

The Act extends and expands existing tax credits to increase domestic production and the sale of components used in wind, solar, fuel cell, hydropower, waste energy, and other clean energy projects, including storage, as well as individual clean energy incentives, including energy rebates and consumer tax credits for energy-efficient homes and vehicles.

One of the most noteworthy changes involves how certain credits can be monetized. Under the Act there is a “direct pay” election in which certain credits are refundable, and/or some credits can be sold for cash without taxation of the sales proceeds. Previously, tax equity investors often had to become partners in a partnership that qualified for and generated the credit to monetize it into cash.

### **IRS Appropriations and Enforcement**

The Act provides approximately \$80 billion of additional IRS funding over the next nine years. More than half of the funds (i.e., over \$45 billion) will be allocated to enforcement efforts, including (i) determining and collecting owed taxes; (ii) providing legal and litigation support; (iii) conducting criminal investigations; (iv) monitoring digital assets and carrying out related compliance activities; and (v) enforcing criminal statute violations and other financial crimes pursuant to internal revenue law. The balance of the funding will be allocated to taxpayer services, operations, and business systems modernization.

*This content is for general information purposes only and does not constitute tax advice.*

*If you have any questions or would like additional information on the topics covered in this alert, please contact your engagement partner.*

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