GUIDEPOST STRATEGIES

MEMORANDUM

To: GuidePost Clients
From: GuidePost Strategies
RE: Key Provisions in the Inflation Reduction Act
Date: **UPDATED: August 7, 2022**

UPDATE: *On Sunday, August 7, the Senate passed H.R. 5376, the "Inflation Reduction Act", as amended by a vote of 51-50 with Vice President Harris as the tie-breaker. We describe the updates to H.R. 5376 throughout this memo, but note that the following amendments were agreed to during its consideration on the Senate floor:*

- **Warner Amendment No. 5488** ("To strike the extension of the limitation on State and local taxes and extend the limitation on excess business losses of noncorporate taxpayers, and for other purposes")
- **Thune Amendment No. 5472** ("To remove harmful small business taxes, and for other purposes")

The House is expected to meet on Friday, August 12th to consider the legislation.

OVERVIEW

On Wednesday, July 27, Senate Majority Leader Chuck Schumer (D-NY) and Senator Joe Manchin (D-WV) announced that they reached an agreement on a **$740 billion** reconciliation package that raises corporate taxes, boosts IRS enforcement, extends Affordable Care Act (ACA) subsidies for three years, and provides for major climate change program funding. In this memo, we outline the major provisions of H.R. 5376[1], the "Inflation Reduction Act."

According to the Senate Democrats' one-page summary of the Inflation Reduction Act, the new proposal will invest approximately **$300 billion** in deficit reduction and **$369 billion** in energy security and climate change programs over the next ten years. Note also that the agreement calls for comprehensive permitting reform legislation to be passed before the end of FY 2022. The summary outlines the following topline estimates:

- The proposal will raise **$739 billion** in total revenue, including through:
    - A 15% corporate minimum tax (Joint Committee on Taxation estimates **$313 billion** will be raised). ***Please note that the modified version of H.R. 5376 scales back this provision.***
    - Prescription drug pricing reform (Congressional Budget Office (CBO)[2] estimates **$288 billion** will be raised).
    - IRS tax enforcement (CBO estimates **$124 billion** will be raised)

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[1] This links to the amendment in the nature of a substitute to H.R. 5376, which reflects the changes to the bill since its initial release.

[2] **Please note that on Saturday, August 6, the CBO sent a letter to Majority Leader Schumer detailing new estimates based on the amended version of H.R. 5376. That letter is available here.**

- Carried interest loophole (Joint Committee on taxation estimates **$14 billion** will be raised). ***Please note that the modified version of H.R. 5376 removes this provision.***

- The proposal will invest **$433 billion** in:
    - Energy security and climate change (**$369 billion**)
    - ACA subsidies extension (**$64 billion**)

KEY TAX PROVISIONS

UPDATE: *As referenced above, the modified version of H.R. 5376 scales back the 15% corporate minimum tax provision and removes the carried interest loophole closure provision. Additionally, the modified version of the bill adds a 1% excise tax on stock buybacks (explained below).*

According to the Senate Democrats' tax summary of the proposal, the two main components would "rebuild the IRS" and impose a 15% corporate minimum tax "to ensure the wealthiest Americans and corporations cannot avoid paying their fair share of taxes."[3] The proposal (as updated):

- Invests **$80 billion** over the next ten years for tax enforcement and compliance, which the CBO estimates will allow the IRS to collect **$203 billion**. This provision appropriates:
    - **$3,181,500,000** for taxpayer services.
    - **$45,637,400,000** for enforcement.
    - **$25,326,400,000** for operations support.
    - **$4,750,700,000** for business systems modernization.

  The funds would remain available until September 30, 2031, and "no use of the funds is intended to increase taxes on any taxpayer with taxable income below $400,000."

- Imposes a 15% domestic tax[4] on "book income" for corporations with more than $1 billion in average annual income over a three-year period. U.S. corporations that are members of a foreign-parented multinational group for any taxable year would need to have earned at least $100 million in such income. Foreign corporations that are engaged in a trade or business with the U.S. will be treated as a separate domestic corporation that is owned by a foreign corporation. This provision would be effective for taxable years beginning after December 31, 2022.

  Additionally, financial statement income would be:
    - Reduced by depreciation deductions.
    - Adjusted to disregard any amount of depreciation expense on a taxpayer's financial statement for a property.
    - Reduced by amortization deductions for wireless spectrum used in the business of a wireless telecommunications carrier and acquired after December 31, 2007, and before the enactment of H.R. 5376.
    - Adjusted to disregard an amortization expense on a taxpayer's financial statement for wireless spectrum.

[3] The 15% domestic tax provision summary outlined in this memo is **based on the *amended version of H.R. 5376*** rather than the initial summary released by the Senate Democrats.
[4] Corporations would be required to pay *the larger of* the minimum tax ***or the statutory corporate tax*** (currently 21%).

The minimum tax would also apply to corporations that have been in existence for less than three years. S corporations, regulated investment companies, and real estate investment trusts would be excluded from the provision.

According to the tax summary of the original Manchin-Schumer proposal, corporations would generally be eligible to claim net operating losses and tax credits against the corporate alternative minimum tax (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 adjusted financial statement income.

- Imposes a 1% excise tax of the fair market value of any stock repurchase in a tax year by a publicly traded U.S. corporation, including any subsidiary that has 50% or more of its stock owned by a corporation. The tax would also apply to stock repurchases of certain foreign corporations by subsidiaries and "expatriated entities." The tax would take effect in 2023.

  Note that the provision exempts stock repurchases that are:
  - Less than $1 million.
  - Contributed to an employer-sponsored retirement plan, stock ownership plan, or similar plan.
  - Part of a reorganization with no gain or loss recognized.
  - Made by a regulated investment company or a real estate investment trust.
  - Treated as a dividend.

KEY PRESCRIPTION DRUG PRICING REFORM PROVISIONS

UPDATE: *On Saturday, August 6, Senate Majority Leader Chuck Schumer (D-NY) announced that the Medicare portions of their prescription drug reform plan survived Senate Parliamentarian vetting. However, a separate pillar penalizing drug companies for raising prices on individuals with private health insurance failed the vetting. Accordingly, this pillar will be excluded from the reconciliation package.*

Additionally, Senate Parliamentarian Elizabeth MacDonough ruled against a separate provision capping out-of-pocket costs for insulin for those with private insurance, though note that this provision was included in the amended version of H.R. 5376 released Saturday afternoon. The modified version also includes an insulin cap for Medicare beneficiaries.

According to the Senate Democrats' prescription drug pricing reform summary of the proposal, "the new [Medicare] negotiation policy will ensure that patients with Medicare get the best deal possible on high-priced drugs and pay cost-sharing for those drugs based on the Medicare negotiated price." The proposal:

- Caps Medicare patients' out of pocket costs at $2,000 per year, with the option to break that amount into affordable monthly payments.
- Institutes a new "inflation rebate" under Medicare, requiring drug companies to rebate back the difference to Medicare if they raise drug prices higher than inflation.
- Puts more financial responsibility on both manufacturers and insurers to keep drug prices down.
- Stabilizes Part D premiums for seniors in Medicare by holding annual premium growth to existing levels.
- Provides free vaccines for seniors.
- Closes a loophole allowing the Secretary to refuse to negotiate or negotiate fewer than the maximum number of drugs by requiring the Secretary to negotiate the maximum number of drugs each year, "to the extent that number of drugs qualify for negotiation."

- Eliminates the partial subsidy status for seniors earning less than 150% of the federal policy level, giving those seniors the full low-income subsidy under Medicare Part D.

KEY ENERGY AND CLIMATE INVESTMENT PROVISIONS

According to the Senate Democrats' energy security and climate change provisions summary of the proposal, "[t]he combined investments in the FY2022 Budget Reconciliation bill would put the U.S. on a path to roughly 40% emissions reduction by 2030, and would represent the single biggest climate investment in U.S. history." The proposal includes provisions that would:

- Help consumers afford technologies aimed at lowering emissions.
- Support energy reliability and cleaner production coupled with "historic investments in American clean energy manufacturing" to lessen reliance on China and create clean-energy manufacturing jobs.
- Invest in decarbonizing all sectors of the economy through "targeted federal support of innovative climate solutions."
- Invest in farmers and forestland owners "to be part of growing climate solutions" to support building resilience for rural communities.

Consumer Incentives for Energy Efficient and Electric Products

The proposal provides for direct consumer incentives to buy energy efficient and electric appliances, clean vehicles, and roof-top solar, and invest in home energy efficiency - with a significant portion of the funding going to lower-income households and disadvantaged communities. The proposal includes:

- **$9 billion** in consumer home energy rebate programs to electrify home appliances and for energy efficient retrofits.
- 10 years of consumer tax credits to make homes energy efficient and run on clean energy, including through heat pumps, rooftop solar, electric HVAC, and water heaters.
- A $4,000 consumer tax credit for lower/middle income individuals to buy used-clean vehicles, and an up to $7,500 tax credit to buy new clean vehicles.
- A **$1 billion** grant program to make affordable housing more energy efficient.

Energy Security and Domestic Manufacturing

The proposal includes **over $60 billion** to on-shore clean energy manufacturing across the full supply chain of clean energy and transportation technologies. The proposal provides:

- Production tax credits to accelerate domestic manufacturing of solar panels, wind turbines, batteries, and critical minerals processing, an estimated **$30 billion** investment.
- A **$10 billion** investment tax credit to build clean technology manufacturing facilities (e.g., facilities to make electric vehicles, wind turbines, and solar panels).
- A **$500 million** Defense Production Act investment for heat pumps and critical minerals processing.
- **$2 billion** in grants to retool existing auto manufacturing facilities to manufacture clean vehicles.
- **Up to $20 billion** in loans to build new clean vehicle manufacturing facilities across the country.
- **$2 billion** for National Labs to accelerate "breakthrough energy research."

Decarbonization

The proposal includes:

- Tax credits for clean sources of electricity and energy storage and **roughly $30 billion** in targeted grant and loan programs for states and electric utilities to accelerate the transition to clean electricity.
- Tax credits and grants for clean fuels and commercial vehicles.
- Grants and tax credits to reduce emissions from industrial manufacturing, including **almost $6 billion** for a new Advanced Industrial Facilities Deployment Program.
- **Over $9 billion** for federal procurement of U.S.-made clean technologies - including **$3 billion** for the U.S. Postal Service to purchase zero-emission vehicles.
- **$27 billion** to accelerate clean energy technology, supporting deployment of emissions-reducing technologies.
- A Methane Emissions Reduction Program to reduce the leaks from the production and distribution of natural gas.

Community Investment

The proposal includes:

- **$3 billion** in grants to reduce air pollution at ports, supporting the purchase and installation of zero-emission equipment and technology at ports.
- **$1 billion** for clean heavy-duty vehicles (e.g., school and transit buses, garbage trucks).

Investment in Rural Community Resilience

The proposal includes:

- **Over $20 billion** in funding for climate-smart agriculture practices.
- Tax credits and grants to support the domestic production of biofuels, and to build the infrastructure necessary for sustainable aviation fuel and other biofuels.

Energy Production Fees

The proposal imposes:

- Waste emission fees for facilities that produce 25,000 metric tons of carbon dioxide each year - **$900** in fees in 2024; **$1,200** in 2025; and **$1,500** in 2026 and beyond.
- A methane fee on metric tons emitted from natural gas and oil production facilities that exceed:
    - 20% of the natural gas sent to sale or
    - Ten metric tons of methane per million barrels of oil sent to sale. The penalty is the same as the waste emissions fees outlined in Section 60113 of the bill.

The proposal also applies oil and gas royalties to extracted methane that is vented or flared, and permanently extends the per ton coal mine operator's tax.