INDIVIDUAL TAX PROVISIONS OF THE INFLATION REDUCTION ACT

THOUGHT LEADERSHIP PERSPECTIVES

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WITH THE PASSING OF THE INFLATION REDUCTION ACT OF 2022, THERE ARE SOME POSSIBLE TAX PLANNING OPPORTUNITIES RELATING TO GREEN ENERGY CREDITS. THE MAJORITY OF THE SPENDING IN THE ACT IS FOR TAX CREDITS ENCOURAGING RENEWABLE ENERGY AND REDUCING EMISSIONS.

This includes an expansion of energy credits available to individual taxpayers: however, one source of funding for the Act that will affect individual taxpayers is the stated goal of increasing Internal Revenue Service audit rates. This has raised concerns of increased audit rates for individuals.

WHAT IS INCLUDED

Energy Efficient Home Improvement Credit

The credit for nonbusiness energy property is extended through 2032. The credit applies to energy efficient windows and doors, certain HVAC systems, and certain heat pumps. The 'old' rules apply for property placed in service during 2022, which means the credit is equal to 26% of the cost. The "new" rules apply for property placed in service during 2023. The credit rate is increased to 30%, however there are additional limitations for certain types of property. The new rules also replace the lifetime maximum credit of $500 with an annual limit of $1,200.

Residential Energy Efficient Property Credit

This credit has been extended through 2034. The credit is 30% for 2022 through the next 10 years, then is reduced to 26% and 22% for 2033 and 2034. This credit is for qualified residential energy efficient property such as solar electric property, solar water heating property, small wind energy property, and geothermal heat pump property.

New Clean Vehicle Credit and Used Clean Vehicle Credit

Credits for 'clean vehicles' are extended through 2032. Clean vehicles include plug-in electric vehicles and fuel cell vehicles. The maximum credit remains at $7,500 for new clean vehicles which is comprised of a $3,750 credit if the vehicle satisfies certain domestic content requirements for critical materials in the battery, and a $3,750 credit if the vehicle satisfies certain domestic content requirements for battery components.

The Act includes income limitations for eligibility for the credit and credit limitations based upon manufacturer's suggested retail price. The credit is not allowed if the taxpayer's modified adjusted gross income exceeds $300,000 for married filing jointly. The credit is also not allowed if the manufacturer's suggested retail price (MSRP) exceeds (1) $80,000 for a van, SUV, or pick-up truck or (2) $55,000 for any other vehicle.

Taxpayers can elect to have the benefit of the credit when they purchase the vehicle, rather than waiting for the filing of the tax return. The car dealer may pay the taxpayer an amount equal to the credit in cash, partial payment, or down payment for the purchase. If the taxpayer receives the credit from the dealer but is ultimately not entitled to the credit (if the modified adjusted gross income is in excess of the threshold), then the taxpayer must include that amount as income.

A credit of up to $4,000 is now available for the purchase of a previously owned clean vehicle starting for the 2023 tax year. The eligibility for this credit is subject to income limitations. The credit is not allowed if the taxpayer's modified adjusted gross income exceeds $150,000 for married filing jointly filers.

Extend the Passthrough Loss Limitations

The Act further extends the excess business loss limitation for Partnerships and S Corporations through 2028.

Increased Funding for the Internal Revenue Service

The Internal Revenue Service (IRS) has had its budget cut over the past decade. That has meant a lack of resources for tasks such as assisting taxpayers with questions, processing returns, and auditing tax returns. There have not been any technology investments or updates.

The Act has allocated $80 billion in funding for the IRS over the next ten years. There will be more funds for new agents, enhanced enforcement, and technology. Much of the new hiring of the 87,000 new agents is to replace the 50,000 retired and soon retiring agents over the next ten years.

On August 10th, Secretary of the Treasury Janet Yellen sent a letter to the Commissioner of the IRS directing that additional funding should not be used to increase the audit rate on small businesses or households below the $400,000 threshold. She calls for enforcement resources to focus on high-end compliance such as large corporations, high-net-worth individuals, and complex pass-throughs.

What could an increased audit rate mean? A greater likelihood that you could be audited. In a best-case scenario, an audit is extremely time consuming but results in no change; however, even in a no change audit, additional time will be spent by taxpayers and/or tax professionals to deal with the audit.

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