At a glance

On August 16, President Biden signed the Inflation Reduction Act (the IRA) into law, which includes implementation of a new alternative minimum tax, an excise tax on stock buybacks, and significant tax incentives for energy and climate initiatives, among other provisions.

On August 9, President Biden signed the Creating Helpful Incentives to Produce Semiconductors (CHIPS) Act into law, which includes an advanced manufacturing investment tax credit, among other provisions.

This In depth does not include a comprehensive discussion of all aspects of the IRA or CHIPS Act. Instead, it is focused only on the provisions of each law that may have accounting implications. We will expand this In depth for additional topics as needed and update it as interpretations evolve.

Accounting for tax law changes

Under US GAAP, changes in income tax rates and law are accounted for in the period of enactment. For US federal purposes, the enactment date for US GAAP is the date the President signs the bill into law.

Although some entities may determine that certain provisions in the IRA require accounting in the period of enactment, the majority of the provisions in the IRA with accounting implications will impact financial statements prospectively. The only aspect of the CHIPS Act that is expected to have an accounting impact will not require any accounting in the period of enactment.

Key provisions of the IRA

Corporate alternative minimum tax

The corporate alternative minimum tax (CAMT) imposes a minimum tax on the adjusted financial statement income (AFSI) for “applicable corporations” with average annual AFSI over a three-year period in excess of $1 billion. A corporation that is a member of a foreign-parented multinational group, as defined, must include the AFSI (with certain modifications) of all members of the group in applying the $1 billion test, but would only be subject to CAMT if the three-year average AFSI of its US members, US trades or business of foreign group members that are not subsidiaries of US members, and foreign subsidiaries of US members exceeds $100 million.
AFSI can generally be described as net income adjusted for certain items. Adjustments include:

- replacing book income, cost, or expense related to a covered benefit plan (e.g., fair value adjustments related to a defined benefit plan) with income or deductions for those covered benefit plans as determined under the tax law,
- replacing the entity’s book depreciation for certain property, plant, and equipment with its depreciation as calculated under the tax law, and
- disregarding federal income taxes.

The IRA imposes a tentative minimum tax equal to the excess of 15% of the applicable corporation’s AFSI over the CAMT foreign tax credit (CAMT FTC) for the tax year. The CAMT is only due if a taxpayer’s tentative minimum tax exceeds its regular tax plus base erosion and anti-abuse tax (BEAT).

Entities that pay tax under the CAMT will receive a tax credit (CAMT credit carryforward) for the tax paid in excess of the amount computed on the basis of the regular tax plus BEAT. The CAMT credit carryforward can be claimed against regular tax in future years (where regular tax plus BEAT exceeds tentative minimum tax) and has no expiration period.

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

**Tax accounting implications**

Prior to US tax reform in 2017, the US had an AMT regime that was explicitly addressed in US GAAP. When there is both a regular tax system and an alternative minimum tax system with the ability to generate a credit against regular tax liabilities in future years, ASC 740 requires deferred taxes to be measured using the regular tax rate even if the company anticipates remaining subject to the AMT system for the foreseeable future (see ASC 740-10-30-10 through 30-11 and ASC 740-10-55-31 through 55-33). Further, ASC 740 provides that a deferred tax asset should be recognized for the AMT credit carryforward. Finally, the guidance also requires companies to consider the realization of the AMT credit carryforward deferred tax asset similar to any other deferred tax asset.

A company’s expectation about being a perpetual CAMT taxpayer may impact its valuation allowance assessment, including the potential need for additional valuation allowance in the period of enactment.

**Excise tax on corporate stock repurchases**

The IRA imposes a nondeductible 1% excise tax on a publicly traded corporation for the net value of certain stock that the corporation repurchases during the tax year.

The value of repurchases subject to the tax is reduced by the value of any stock issued by the corporation during the tax year, including stock issued or provided to the employees of the corporation or employees of a specified affiliate of the corporation during the tax year, whether or not such stock is issued or provided in response to the exercise of an option to purchase such stock. Additional exceptions are noted in the law.

The provision includes special rules for foreign-parented domestic corporations that would treat a repurchase of stock by certain affiliates of a publicly traded foreign corporation (including domestic corporations,
domestic partnerships, and foreign partnerships with domestic partners) as if it were a repurchase by a publicly traded US corporation.

This provision would apply to repurchases of stock after December 31, 2022.

**Accounting implications**

Taxes that are not based on income are outside the scope of ASC 740. Because the excise tax is levied on the gross amount (i.e., the tax basis excludes any expenditures or other adjustments), the effects of the excise tax are not expected to be included in an entity’s income tax provision under ASC 740.

US GAAP does not contain explicit guidance for taxes that are not subject to ASC 740, but most transactional taxes – excise taxes, sales taxes, value-added taxes, etc. – are reflected as an additional cost of the underlying pre-tax transaction that gives rise to the tax. Under US GAAP, many stock repurchases are accounted for as equity transactions with no income statement consequence, although certain equity transactions may have income statement consequences and not all equity shares are classified as equity instruments. As a result, the US GAAP accounting treatment for a stock buyback transaction may be relevant in determining the appropriate accounting for the tax cost.

**Climate and clean energy provisions**

The IRA includes significant extensions, expansions, and enhancements of numerous energy-related tax credits and also creates new credits in multiple categories, including advanced manufacturing production credits and credits for clean production of electricity, fuel, hydrogen, and nuclear power.

Certain of the credits have a “direct-pay election” which allows an eligible taxpayer to receive a current benefit from the credit without taxable income or a tax liability. What constitutes an “eligible taxpayer” varies depending on the credit, but for most of the credits, the population of taxpayers eligible for the direct-pay option is fairly narrow and limited generally to tax exempt and governmental entities as well as rural electric cooperatives.

The law also provides an election to transfer (i.e., sell) certain credits to another taxpayer. The transfer may be for all or a portion of a credit, but any credit may only be transferred once. The cash received in exchange for the credits transferred is not includable in taxable income of the transferor nor deductible to the transferee. For most of the credits, the population of entities that can elect to transfer the credit is broader than the population of entities that could elect the direct-pay option, which may cause the transfer election to be more common.

The provisions with respect to the impacted credits have various effective dates. The option for direct-pay and transferability of credits will apply to taxable years beginning after December 31, 2022.
**Accounting implications**

The application of the ASC 740 income tax accounting model is warranted if a particular credit or incentive can only be claimed on the income tax return and can be realized only through the existence of taxable income. When a company is able to receive the benefit of a credit regardless of whether it has income taxes payable or taxable income, we believe the benefit should be accounted for outside of the income tax model. This would apply to credits with a direct-pay option.

For credits that a taxpayer can opt to transfer to another taxpayer, the entity that generated the credit should consider how they intend to monetize the credit. If the entity does not intend to transfer the credit, and therefore will only realize the benefit of the credit by reducing its income tax payable, it would account for the benefit of the credit as part of its income tax provision determined under ASC 740. However, if the entity intends to realize the benefit of the credit by transferring it to another party, it should account for initial recognition of the benefit of the credit and the transfer of the credit outside of the income tax line.

When credits are not accounted for under the income tax model in ASC 740, a reporting entity will need to determine the appropriate accounting framework to apply. The direct-pay and transferability provisions make many of these credits akin to a government grant or subsidy. Although the FASB has an active project on its agenda on the accounting for government assistance, there is currently no US GAAP that explicitly addresses the accounting by business entities for government assistance. As a result, reporting entities generally analogize to either ASC 958-605, *Not-for-profit entities—Revenue recognition*, or IAS 20, *Accounting for Government Grants and Disclosures of Government Assistance*.

In practice, most for-profit business entities apply an IAS 20 approach to the recognition of government assistance. When applying the IAS 20 accounting model to tax credits in the IRA, a reporting entity will need to identify, understand, and evaluate all conditions of the credits for which it may be eligible to determine when the credit should be recognized in the financial statements. Several of the energy-related tax credits include specific conditions related to prevailing wages and apprenticeships, domestic content, and/or critical minerals. If these conditions are met, the taxpayer will be able to claim a bonus credit rate instead of the base credit rate. The requirements of the relevant credits will determine the appropriate amounts to recognize in the financial statements.

Income statement classification of the income from a tax credit will vary depending on the facts and circumstances that give rise to the credit and will sometimes be reported as other income while at other times it may be reported as a reduction to the related expenditures that generated the credit. See section 10 in our *In depth* on accounting for COVID-19 and market volatility for additional details on the accounting for government assistance.
Key provision of the CHIPS Act

Advanced manufacturing investment tax credit

The CHIPS Act provides a credit of 25% of an eligible taxpayer’s qualified investment in an advanced manufacturing facility. Similar to certain of the energy credits in the IRA, a taxpayer may make an irrevocable election to treat the credit as a payment against tax, thus electing the direct-pay option.

The credit will be subject to recapture for taxpayers that dispose of the property prior to five years after the credit was generated.

The credit applies to qualified property placed in service after December 31, 2022, for which construction begins before January 1, 2027.

Tax accounting implications

As described under the IRA credit provisions, because this credit is refundable to the taxpayer even if the taxpayer does not have taxable income or a tax liability, it is more akin to a government grant and should therefore be accounted for outside of the income tax provision.

What’s next

We expect that certain provisions of these tax laws will be the subject of further guidance from Treasury in the months ahead. Entities should monitor developments in the law and assess any potential accounting impacts as the guidance continues to evolve.

To have a deeper discussion, contact:

Jennifer Spang
Partner
Email: jennifer.a.spang@pwc.com

Matt McCann
Partner
Email: matthew.j.mccann@pwc.com

Kassie Bauman
Managing director
Email: kathleen.bauman@pwc.com

Nicole Siroonian
Senior manager
Email: nicole.l.siroonian@pwc.com

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