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Annual Conference Scottsdale, AZ

The Inflation Reduction Act's
Book Minimum Tax –
Introduction and Hot Topics

October 24, 2022



- Minimum tax of 15% of any “applicable corporation’s” “adjusted financial statement income” (“AFSI”)
- Effective in taxable years beginning after December 31, 2022
- Applicable corporations are generally those with average annual AFSI of over \$1 billion
 - In the case of foreign-parented multinational group, worldwide group average annual AFSI of over \$1 billion, and a U.S. group member with average annual AFSI of at least \$100 million
- AFSI starting point is net income set forth on “applicable financial statement” for the taxable year

“Applicable Financial Statement”

- Defined in Code section 451(b)(3). In most cases:
- A financial statement certified as being prepared in accordance with GAAP and which is:
 - A 10-K;
 - If no 10-k, an audited financial statement used for credit purposes, for reporting to shareholders, partners, etc., or for any other substantial nontax purpose; OR
- A financial statement made based on international financial reporting standards (“IFRS”) and filed with the foreign equivalent of the SEC, if the corporation has no GAAP financial statement

- Adjustments from financial statement net income in computing AFSI include:
 - Disregard federal and foreign income taxes
 - Carve-outs to allow for MACRS depreciation, tax treatment of pension and other defined benefit plans, tax amortization with respect to wireless spectrum
 - Regulatory authority to make other adjustments, for example to address corporate liquidations, reorganizations, and partnership contributions and distributions
- Financial statement NOLs (including for 2020, 2021, and 2022) can be carried forward and applied against up to 80% of AFSI in future years
- Business credits (research credit, energy credits, etc.) are allowed against BMT
- Prior year BMT can be credited against the excess of regular tax (plus BEAT) over BMT in future years

- AFSI of consolidated groups determined on group basis from group's financial statement
- AFSI of non-consolidated corporations (other than CFCs) is not included in corporate owner's AFSI – only dividends and gains are included
- If corporation is partner, AFSI includes only distributive share of AFSI of partnership
- AFSI includes AFSI of any disregarded entity owned by corporation

- AFSI of CFCs, exclusive of foreign taxes, is included based on financial statement of each CFC
 - Any net loss from CFCs cannot be used to reduce AFSI of the U.S. taxpayer, but can be carried forward and applied against future inclusions of AFSI
- Indirect BMT foreign tax credit of up to 15% of CFC AFSI
 - No basketing
 - No limitation to 80% of foreign taxes
 - Excess credits can be carried forward
- Unlimited direct BMT foreign tax credit

“Applicable Corporation” – U.S. Parented Groups

- Any corporation (other than an S corporation, a RIC, or a REIT) which meets the “average annual AFSI” test for one or more prior taxable years which end after December 31, 2021
- Average Annual AFSI test
 - Average annual AFSI for the 3 taxable year period ending with such taxable year exceeds \$1 billion

“Applicable Corporation” – Foreign Parented Groups

- Solely for purposes of determining whether the corporation meets the Average Annual AFSI test, AFSI of corporation includes AFSI of all members of the group
- Corporation is an applicable corporation if:
 - Group meets average annual AFSI test; and
 - Taxpayer itself has average annual AFSI for the 3 taxable year period ending with such taxable year of \$100 million or more

Applicable Corporation - Exception

- Corporation:
 - Has a change in ownership; OR
 - Has a “specified number” (to be determined by IRS, apparently on a case-by-case basis), of consecutive taxable years in which the corporation does not meet the annual adjusted AFSI test, AND
- IRS determines that it would not be appropriate to continue to treat the corporation as an applicable corporation

Applicable Corporation - Aggregation Rule

- Solely for purposes of determining whether a corporation is an applicable corporation, all AFSI of persons treated as a single employer with such corporation under subsection (a) or (b) of section 52 treated as AFSI of such corporation
- Subsection (a) covers controlled groups of corporations including:
 - Parent-subsidiary controlled groups (chains of corporations connected through more than 50% stock ownership with a common parent corporation)
 - Brother-sister controlled groups (5 or fewer persons who are individuals, estates or trusts own more than 80 percent of each corporation, and 50 percent of each corporation in identical shares)
 - Subject to constructive ownership rules in section 1563(d) and (e)
- Subsection (b) (and Treas. Reg. § 1.52-1) cover “trades or businesses [such as sole proprietorships and partnerships] that are under common control,” including a “parent-subsidiary group under common control” or a “brother-sister group under common control”

BMT – International Aspects

- Pro rata share of CFC income included in AFSI
- Foreign financial statement is the relevant financial statement for inclusion
- Loss offsets:
 - CFC to CFC OK
 - Net CFC loss cannot offset US AFSI
 - US AFSI loss can offset CFC AFSI

BMT – International Aspects

- BMT foreign tax credit
 - Available up to 15% of CFC AFSI
 - No basketing
 - Blending OK
 - No GILTI haircut
 - Carryforward available

BMT – International Aspects

- Technical issues – lots of need for Treasury guidance
 - Double-counting of CFC dividends
 - Foreign tax credits:
 - Fiscal year issues
 - Impact of new FTC regulations and creditability issues
- Treasury guidance process

BMT – International Aspects

- BMT and Pillar 2 - “What we have here is a failure to communicate.”
 - BMT as a covered tax – rate, blending, credits
 - EU Commissioner comments
 - Relationship to GILTI
 - Consequences of US non-compliance

- The BMT has no impact on the effective tax rate (before valuation allowance (“VA”) considerations)
 - BMT is a period expense
 - Tax credit received for BMT paid is a deferred tax benefit
- Deferred tax assets and liabilities are to be measured using the regular tax rate of 21% even if taxpayer expects to pay BMT in perpetuity (ASC 740-10-30-10 through 30-11)
- The IRA amended the General Business Credit (“GBC”) limitation to allow GBCs to be used against both the regular tax liability and the BMT, preserving the value of GBCs

ASC 740 Valuation Allowance Considerations

- Should the effects of being subject to the BMT in the future be considered when assessing the realizability of deferred tax assets (“DTA”)?
 - For DTAs other than the BMT credit, FASB indicates an accounting policy election can be made (applicable to new BMT only)
 - Potential for a change in the VA in the period that includes the August 16, 2022 enactment date
 - For BMT credit, expectation of BMT status should be considered
 - Taxpayer expecting to be in BMT in perpetuity might find it difficult to conclude they are more likely than not to realize the benefit of the BMT credit carryforward
- Any recognition of VA for the BMT credit causes the BMT to impact the effective tax rate

