



US International Tax Alert

Corporate AMT Included in Inflation Reduction Act of 2022

Overview

On August 7, 2022, the Senate passed the Inflation Reduction Act of 2022. The bill includes a book-minimum tax (corporate AMT) similar to that originally proposed in the Build Back Better Act¹ that would impose a 15% minimum tax on “adjusted financial statement income” (AFSI) of applicable corporations over the “corporate AMT foreign tax credit for the taxable year.” The House is expected to approve the legislation on August 12, after which it will be signed into law by President Biden. The proposal would be effective for taxable years beginning after December 31, 2022.

Under the bill, an applicable corporation’s minimum tax would be equal to the amount by which the tentative minimum tax exceeds the sum of corporation’s regular tax for the year and the corporation’s BEAT liability under section 59A.

Observation: Once a corporation is determined to be an applicable corporation, it remains an applicable corporation in perpetuity, subject to limited exceptions discussed below.

Although similar to other proposed legislation (see prior coverage of the tax provisions of the Build Back Better Act), the current bill includes a few notable modifications, including:

URL: <https://www2.deloitte.com/content/dam/Deloitte/us/Documents/Tax/us-tax-provisions-in-the-build-back-better-act.pdf>

- A modification to the language addressing the amount of income that is taken into account and attributable to the holding of stock in a corporation that is not a member of the US consolidated group. In such cases, AFSI of the taxpayer with respect to such corporation shall be determined by only taking into account the dividends received from such other corporation. It is our understanding this adjustment is intended to exclude amounts otherwise taken into account *with respect to stock* under the mark-to-market method of accounting.
- A special rule addressing the treatment of amounts attributable to defined benefit pension plans and tax-exempt income.

¹ H.R. 5376, 117th Cong. § 138126.

- Provisions allowing for reductions to AFSI for (i) depreciation deductions allowed under section 167 with respect to section 168 property and (ii) amortization deductions allowed under section 197 with respect to “qualified wireless spectrum.” When these provisions are applicable, AFSI is adjusted to disregard any amount of depreciation or amortization expense that is taken into account in the taxpayer’s applicable financial statement with respect to such property and qualified wireless spectrum and substitute the amount taken into account in computing regular tax.

Determination of applicable corporation

An applicable corporation is any corporation (other than an S corporation, regulated investment company, or a real estate investment trust) that meets the \$1 billion three-year average annual AFSI test, applied based on a three-year look-back period ending with the relevant taxable year. Under the proposed provisions, a corporation can first qualify as an applicable corporation in a taxable year ending after December 31, 2021.

Once a corporation is determined to be an applicable corporation, it remains an applicable corporation unless, as a result of an ownership change or a consistent reduction in AFSI below a yet-to-be-determined applicable threshold, the Secretary determines that it would not be appropriate to continue to treat such corporation as an applicable corporation.

Observation: The legislative text does not provide any guidance as to what quantum of ownership change is necessary or the length of the period during which the \$1 billion AFSI threshold is not met to trigger this exception.

In general, although the determination of whether a corporation is an applicable corporation is based on AFSI, special rules are included for computing AFSI for this purpose.

First, in the case of a foreign-parented multinational group,² the \$1 billion three-year average annual AFSI requirement is determined by aggregating the AFSI for all members of the foreign-parented multinational group in which the applicable corporation is a member. However, if the foreign-parented multinational group meets this \$1 billion requirement, a domestic corporation (or foreign corporation with a US trade or business) that is a member of that group is not treated as an applicable corporation unless it meets an additional \$100 million threshold, determined without regard to the expanded AFSI rule relevant for purposes of determining whether the \$1 billion threshold is met. When applicable, the corporation will only be subject to tax under the corporate AMT on the AFSI computed with respect to the domestic corporation (or foreign corporation with a US trade or business) and not on the aggregated AFSI determined with respect to all members of the foreign-parented multinational group.

² For purposes of this rule, the term foreign-parented multinational group means, with respect to any taxable year, two or more entities if: (i) at least one entity is a domestic corporation (or a foreign corporation engaged in a US trade or business); (ii) such entities are included in the same applicable financial statement with respect to such year; and (iii) the common parent is a foreign corporation or, if there is no common parent, the entities are treated as having a common parent that is a foreign corporation under regulations prescribed by the Secretary.

Observation: Although the determination of whether an entity is an applicable corporation can take into account income of all foreign corporations, regardless of whether the United States can subject such foreign corporations to tax, the liability for the corporate AMT applies *solely* with respect to domestic corporations or foreign corporations that have ECI (*i.e.*, the foreign corporations that do not have ECI do not have corporate AMT liability).

Second, and 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 section 52(a) or (b) is treated as AFSI of such corporation. Earlier versions of the bill included an expansion of the term trade or business under section 52, beyond any trade or business as determined under section 162, to include both:

1. Any activity involving research and experimentation activity under section 174 and
2. Any activity giving rise to deductions allowable under section 212.

An additional clarification was made to section 52(a). *However, such expansions were struck prior to final passage by the Senate.*

Observation: The legislative text suggests that for purposes of determining whether a corporation is an applicable corporation, the corporation needs to include all of a partnership's AFSI to the extent the corporation and the partnership are treated as a single employer under section 52(b), as opposed to looking to the corporation's distributive share of such income. In addition, in certain cases, a corporation may consolidate a partnership for financial statement purposes even if the corporation and the partnership are not treated as a single employer under section 52(b). Further analysis may be required in this situation to determine whether the corporation is an applicable corporation.

Computation of AFSI

Tentative minimum tax is determined by applying a 15% tax rate to the AFSI of the corporation for the taxable year (computed taking into account financial statement net operating losses) reduced by the corporate AMT foreign tax credit. For this purpose, AFSI is the net income or loss of the taxpayer stated on the taxpayer's applicable financial statement³ with certain modifications, including adjustments to:

1. Align the period covered to the taxpayer's taxable year,
2. Disregard any federal or foreign income taxes taken into account, and
3. Disregard any direct payments made with respect to certain tax credits.

The bill includes a provision for computing AFSI for an applicable corporation that is a partner in a partnership. Under this rule:

If the taxpayer is a partner in a partnership, except as provided by the Secretary, AFSI of the taxpayer must be adjusted to only take into account the taxpayer's distributive share of AFSI of such partnership.

³ The term applicable financial statement means, with respect to any taxable year, an applicable financial statement (as defined in section 451(b)(3) or as specified by the Secretary in regulations or other guidance) that covers such taxable year.

- The AFSI of a partnership is the partnership's net income or loss set forth on such partnership's applicable financial statement (with certain modifications, as described above). Importantly, further analysis may be required to the extent a partnership does not have an applicable financial statement (*e.g.*, if the partnership is included on the corporation's financial statements).

Observation: Even where a corporation includes all of a partnership's AFSI to determine whether a corporation is an applicable corporation (*e.g.*, if the corporation and the partnership are treated as a single employer under section 52(b) or are consolidated for financial statement purposes), the amount of AFSI actually used to compute the corporation's AMT tax liability appears to be limited to the corporation's distributive share of the partnership's AFSI.

The bill also includes a number of other rules including:

- As discussed above, a provision applicable to corporations that are not included in a consolidated return of the taxpayer. In such a case, AFSI of the taxpayer with respect to such corporation shall be determined by only taking into account the dividends received from such corporation (reduced to the extent provided by the Secretary in regulations) and other amounts which are includible in gross income or deductible as a loss under this chapter (other than amounts included under section 951 or 951A or such other amounts as provided by the Secretary) with respect to such other corporation.

Observation: As stated above, it is our understanding that this adjustment is intended to ensure that amounts included in the AFSI of a corporation *with respect to stock* under the mark-to-market method of accounting are not taken into account for purposes of computing AFSI under the corporate AMT. However, there remains an open question as to whether and how this provision might apply to mark-to-market gains on partnership interests.

- In the case of a corporation that is a US shareholder of a controlled foreign corporation (CFC), AFSI includes the corporation's pro rata share of the AFSI of such CFC. For this purpose, the AFSI of CFCs are aggregated globally and a loss by one CFC may offset income of another CFC. However, net overall losses of CFCs may not reduce AFSI of a US corporation but may be carried forward and used to offset the global CFC AFSI in future years.
- Rules that provide adjustments with respect to defined benefit pensions. Under these provisions, and except as otherwise provided by the Secretary, AFSI shall be: (i) adjusted to disregard any amount of income, cost or expense that would otherwise be includible on the AFSI with respect to any covered benefit plan⁴; (ii) increased by any amount of income in connection with any covered benefit plan that is included in the gross income of the corporation; and (iii) reduced by

⁴ A covered benefit plan means: (i) a defined benefit plan (other than a multiemployer plan described in section 414(f)) if the trust which is part of such plan is an employees' trust described in section 401(a) which is exempt from tax under section 501(a); (ii) any qualified foreign plan defined in section 404A(e); or (iii) any other defined benefit plan which provides post-employment benefits other than pension benefits.

deductions allowed with respect to such covered benefit plan.

- Rules applicable to certain cooperatives and Alaska Native Corporations and to provide consistent treatment with respect to mortgage servicing income of a corporation other than a regulated investment company.
- Rules to adjust AFSI in the case of a tax-exempt entity, such that AFSI only takes into account income that is: (i) income of an unrelated trade or business under section 513, or (ii) income derived from debt financed property (as defined in section 514) to the extent that income from such property would be unrelated business taxable income.
- Modifications to AFSI with respect to depreciation deductions under section 167 with respect to property to which section 168 applies. In such a case, AFSI shall be reduced by any depreciation deductions under section 167 with respect to property to which section 168 applies and appropriately adjusted to disregard any amount of depreciation expense that is taken into account on the taxpayer's applicable financial statement. Other items may be also adjusted by the Secretary.

Observation: The apparent intent of this rule is to substitute amounts used in computing taxable income for purposes of computing regular tax liability for amounts reflected on the applicable financial statement and, thereby, preserve the deductions and avoid timing differences for computing *both* corporate AMT and regular tax.

- Modifications to AFSI with respect to amortization deductions under section 197 solely with respect to qualified wireless spectrum.⁵ In such a case, AFSI shall be reduced by any amortization deductions under section 197 with respect to qualified wireless spectrum and appropriately adjusted to disregard any amount of amortization expense that is taken into account on the taxpayer's applicable financial statement with respect to qualified wireless spectrum.

Observation: The apparent intent of this rule is to substitute amounts used in computing taxable income for purposes of computing regular tax liability for amounts reflected on the applicable financial statement and, thereby, preserve the deductions and avoid timing differences for computing both corporate AMT and regular tax. This rule appears limited to section 197 amortization with respect to qualified wireless spectrum, and presumably would not apply to any other section 197 amortization of the corporation.

The Secretary is also granted regulatory authority to provide adjustments to:

1. Prevent the omission or duplication of any item,
2. Appropriately address corporate liquidations and reorganizations, and
3. Transactions related to partnership contributions and distributions.

Further, special rules apply in the case of related corporations included on a consolidated financial statement and in the case of taxpayers filing a consolidated return. Lastly, the Secretary is granted authority to provide

⁵ Qualified wireless spectrum means wireless spectrum that is used in the trade or business of a wireless telecommunications carrier and was acquired after December 31, 2007, and before the date of enactment of the AMT.

regulations and other guidance as necessary to carry out the purpose of section 56A, including regulations and other guidance relating to the effect of the rules of the section on partnerships with income taken into account by an applicable corporation.

Treatment of financial statement net operating losses

As under the rules applicable to the regular corporate income tax, AFSI may be reduced by financial statement net operating losses, not to exceed 80% of AFSI determined before taking into account such net operating losses. Financial statement net operating losses are determined by taking into account adjusted financial statement losses for taxable years ending after December 31, 2019.

Treatment of foreign income taxes paid or accrued

Tentative minimum tax may be reduced by a corporate AMT foreign tax credit, which takes into account foreign income taxes that are paid or accrued (for federal income tax purposes) and taken into account on an applicable financial statement. For purposes of this provision, foreign income taxes paid or accrued by CFCs are subject to a single global limitation equal to 15% of the net aggregate AFSI of CFCs, while foreign income taxes paid or accrued directly by a domestic corporation, such as withholding taxes or the taxes paid on income of a foreign activity conducted directly by the corporation, are not subject to a limitation. Excess corporate AMT foreign tax credits attributable to CFCs may be carried forward for five years.

Observation: As drafted, the corporate AMT foreign tax credit carryforward appears to apply only to CFC-level foreign taxes in excess of the CFC-specific limitation, rather than global foreign taxes in excess of the overall corporate AMT liability. As a result, it does not appear that any foreign income taxes paid or accrued directly by a domestic corporation would be allowed as a carryforward.

Other credits

As under the current rules, general business credits of a corporation (such as research and development, clean energy, and housing tax credits) may generally offset up to approximately 75% of the sum of a corporation's normal income tax and AMT.

As with the AMT tax credit under the pre-2018 corporate AMT and the AMT currently in effect for individuals, corporations would be eligible to claim a tax credit for AMT paid in prior years against regular income tax, to the extent regular tax exceeds the tentative minimum tax for such taxable year.

Relationship to OECD Pillar Two rules

The Inflation Reduction Act does not modify section 951A to align with definition of a "qualified income inclusion rule" (IIR) in the OECD Pillar Two Model Rules,⁶ as was proposed in Build Back Better. The OECD Pillar Two Model Rules also allow countries to adopt "qualified domestic minimum top-up taxes" (QDMTTs) in order to collect top-up tax that would otherwise be

⁶ See OECD (2021), *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS*, OECD, Paris, <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm>.

allocated to a different jurisdiction. A QDMTT must generally provide outcomes similar to those under the Model Rules. The Biden administration proposed the adoption of a QDMTT in its Greenbook, but no such provision is included in the Inflation Reduction Act.⁷

The AMT shares some similarities with an IIR and QDMTT, such as using financial statement income as the tax base and imposing a 15% minimum rate. Major discrepancies exist, however, such as the worldwide aggregate tax base under the AMT as opposed to the jurisdictional computation under the OECD Pillar Two Model Rules, and the inclusion of deferred taxes when determining whether the taxpayer is required to pay a top-up tax for purposes of the OECD Pillar Two Model Rules.

Observation: Because of the significant differences between the AMT and the OECD Pillar Two Model Rules, it appears unlikely that the AMT would constitute either an IIR or a QDMTT. However, any AMT paid in a year would likely increase covered taxes for purposes of the OECD Pillar Two Model Rules (which would appear to make the application of the IIR or UTPR to such domestic corporation less likely). However, several open issues remain, including whether and how any of the tax paid is “pushed down” to a CFC, and whether AMT credits reduce covered taxes in the year in which they are utilized.

Financial statement considerations (US GAAP)

While we are continuing to analyze the tax, we currently anticipate that the AMT may be accounted for similar to the pre-2018 US corporate AMT. More specifically, ASC 740 addressed the pre-2018 US corporate AMT and provided that “[i]n the U.S. federal tax jurisdiction, the applicable tax rate [for measuring U.S. federal deferred taxes] is the regular tax rate” and a deferred tax asset would be recognized for alternative minimum tax credit carryforwards available under the bill if realization is more likely than not. Accordingly, under this approach, the tax effects of the new AMT would not be reflected in a company’s financial statements until after the bill is effective.



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⁷ See General Explanations of the Administration’s Fiscal Year 2023 Revenue Proposals, <https://home.treasury.gov/system/files/131/General-Explanations-FY2023.pdf>.