AFSCME Facts

New Fair Tax Rules Included in the Inflation Reduction Act
Aug. 16, 2022

Signed by President Biden on Aug. 16, 2022, the Inflation Reduction Act of 2022 (IRA) takes major steps toward requiring big corporations and wealthier people to pay their fair share of taxes, while lowering the national deficit by more than $300 billion. It also includes important changes that lower health care costs, address climate change and invest in energy security. This fact sheet describes the IRA's new fair tax rules.

How does the IRA's corporate minimum tax help stop corporations from avoiding their fair share of taxes?

The IRA creates a new 15% alternative minimum tax for large corporations. It applies to US corporations that have a three-year average income greater than $1 billion and to foreign corporations with a three-year average income in the US greater than $100 million.

Although federal law currently puts a 21% flat tax on corporate income, corporations avoid taxes by using tax shelters and loopholes, such as by recharacterizing their income as coming from another country with lower taxes. That is why very profitable corporations end up paying low or no federal corporate income taxes. For example, 55 profitable corporations with more than $40 billion in US income paid no federal income tax in 2020, according to an analysis by the Institute on Taxation and Economic Policy. Although the IRA does not get rid of every tax shelter and loophole, it will raise an additional $222 billion in taxes from corporations over 10 years.

How are corporate stock buybacks taxed under the IRA?

The IRA puts a 1% tax on stock buybacks. This is a big deal because the US has never taxed corporate profits in this way, and this makes it much harder for corporations to avoid paying taxes by setting up tax shelters and engaging in other schemes. This tax is expected to raise $76 billion over 10 years.

A stock buyback is when a corporation uses its income, assets or both to buy shares of its own stock back from some investors. Doing this benefits the remaining shareholders because it increases the value of the corporation's remaining shares by shrinking the supply of outstanding shares available for investors to buy. One reason why corporations do this is to return earnings back to US shareholders in a form that, unlike dividend payments, is not immediately taxable. Shareholders only get taxed when they sell their stock, and they and their heirs never get taxed if the shareholders hold it until they die and then pass it on to their heirs. Foreign shareholders are never taxed in the US when corporate earnings are passed back to them in this way.

<u>What does the IRA do to make sure corporations and wealthy earners pay what they owe?</u>

The IRA gives the IRS more funding to enforce the laws on the books for corporations and wealthier people. This funding is expected to increase net tax collections from corporations and wealthier people by $124 billion over 10 years. These additional enforcement resources will be used to increase audit rates only for businesses and individual taxpayers with incomes of $400,000 or more, according to a directive from Treasury Secretary Janet Yellen to the IRS commissioner. This added funding is necessary because over the last decade, Congress has not given the IRS the money it needs to keep up with its mission. That is a story many AFSCME members know all too well from their own jobs as governments have failed to hire enough workers and provide enough funding to serve the public effectively.

You can see how badly cuts in IRS funding have hurt its ability to enforce the law and serve the public by looking at the big drop in IRS employees and in audits of corporations and millionaires. According to the Center on Budget and Policy Priorities (CBPP), the total number of IRS employees fell 22% (-21,000) from 2010-2021. This includes a 31% decline (-15,000) in enforcement staff. Also, according to CBPP, the audit rate (i.e., the share of people whose returns get checked in a year) for people earning $1 million or more per year fell by 71% from 2010-2019, significantly more than the drop in the overall audit rate (58%). For big corporations, the audit rate fell by 54%.

<u>What does the IRA do to make it easier for regular taxpayers at tax time?</u>

The IRA provides additional money to improve other services and supports, including $3.2 billion over 10 years to improve taxpayer services and $25.3 billion to improve technology and overall operations. This money will go to hire more workers to answer taxpayer phone calls and provide help to people when they are filing their taxes, among other things. Taxpayer help is another area that has taken a big hit in recent years due to the lack of funding and staff. According to a 2020 IRS report, the agency was only able to answer one in five phone taxpayer phone calls.