August 2022

Inflation Reduction Act of 2022 (IRA)

The Inflation Reduction Act of 2022 (IRA) was signed into law on August 16th after the bill was passed in Congress earlier in the month. Although the most significant provisions of this legislation are primarily directed at corporations and commercial activities, there are several provisions that may affect individuals. The following content outlines the provisions SilverOak has identified as the most likely to impact individual taxpayers directly.

Residential Energy Tax Credits

Energy Efficient Home Improvement Credit

The personal credit for non-business energy property expenditures, which expired at the end of 2021, has been reinstated in its current form through 12/31/2022. Typical improvements qualifying for this credit are energy-efficient insulation, windows, doors, water heaters, heat pumps, a/c units, furnaces, and circulating fans. Given the prior credit has a lifetime limit of $500, anyone who previously reached the lifetime limit will continue to be ineligible in 2022.

Effective 1/1/2023, the amount of the credit will be raised from 10% to 30% of the cost of qualifying residential property improvements and expenditures made through 12/31/2033. Most notably, the existing $500 lifetime limit for this credit has been replaced with a $1,200 annual limit, allowing homeowners to claim a credit for continued expenditures and improvements each year. If a taxpayer has improvements related to qualifying heat pumps, water heaters, or biomass stoves and boilers, a larger credit up to $2,000 can be claimed for the year the improvements are made.

The legislation also modifies the energy efficient certification requirements for what is considered part of the building envelope, which allows for a credit up to $150 for the cost of a home energy audit, and expands the credit so taxpayers can now claim the credit for improvements made on properties other than the taxpayer's primary residence.

Starting in 2025, taxpayers will be required to provide qualified product identification numbers on their tax returns to claim this credit.

Residential Clean Energy Credit

The residential energy efficient property (REEP) credit has also been expanded, with the applicable credit rate for property placed in service in 2022 increasing from 26% to 30%. This applicable credit rate will continue through 2032, with 4% declines in each of the following two years.

Effective 1/1/2023, qualified expenditures for this credit have also been expanded to include battery storage technology expenditures. Typical improvements qualifying for this credit are solar electric property, solar hot water property, fuel cells, geothermal heat pump property, small wind energy property, and qualified biomass fuel property installed in any of the principal or secondary residences.

Electric Vehicle Tax Credits

Clean Vehicle Credit

In addition to redefining the definition of a qualifying vehicle, the new credit has also eliminated the prior 200,000 cars per manufacturer limitation. Thus, any vehicle manufacturer that had previously reached the credit phase-out becomes eligible for any qualifying vehicles purchased and delivered after 12/31/2022. All eligible electric vehicles acquired and delivered in 2022 must continue to qualify under the prior electric vehicle credit.

The new clean vehicle credit is now a two part credit. Taxpayers receive a credit of $3,750 if the vehicle meets the critical minerals requirements, and another $3,750 credit if the vehicle meets the battery component requirement. Each of these credits is available if the applicable percentage of critical minerals or components used in the manufacture of a new electric vehicle's battery meets the following minimum threshold depending on the year the car was put into service:

- Through 2023 - Critical Minerals - 40%; Battery Components - 50%
- 2024 – Critical Minerals - 50%; Battery Components - 60%
- 2025 – Critical Minerals - 60%; Battery Components - 60%
- 2026 – Critical Minerals - 70%; Battery Components - 70%
- 2027 – Critical Minerals - 80%; Battery Components - 80%
- 2028 – Critical Minerals - 80%; Battery Components - 90%
- 2029 & After – Critical Minerals - 80%; Battery Components - 100%

For the critical mineral credit, the above percentages of critical minerals in a car's battery must have been extracted, processed, or recycled in the United States or any nation with which the United States has a free trade agreement. For the battery component credit, the above percentages pertain to the percentage of battery components manufactured or assembled in North America. The final assembly of a vehicle must also occur in North America for it to qualify for either credit. This includes all vehicles purchased after 8/16/2022 and delivered by 12/31/2022, even though they must claim the prior electric vehicle credit in 2022.

Sellers will now be required to provide the buyer and Treasury with a report for vehicles eligible for this tax credit. Given the complexity in determining if a new vehicle qualifies for this credit, buyers must work closely with the dealership when acquiring a vehicle intended to qualify for this credit. Taxpayers will also continue to be required to report vehicle information on their tax return the year they claim the tax credit. Starting in 2024, taxpayers can also elect to transfer the tax credit to qualifying dealers at the time of purchase.

The credit is not intended for higher-end cars, as the manufacturer's suggested retail price (MSRP) for new vehicles must not surpass certain thresholds to qualify for the credit. The MSRP for vans, SUV's, and trucks must not exceed $80,000 for a vehicle to qualify, while all other vehicles have an MSRP limitation of $55,000 to qualify. A taxpayer's modified gross adjusted income must also not exceed certain thresholds to claim the credit: $300,000 for a joint return or surviving spouse, $225,000 for a head of household, and $150,000 for all others. Please note that the income limitations apply for both the year of acquisition and the year before the acquisition. In addition, taxpayers may not claim more than one clean vehicle credit per tax year.

Previously Owned Clean Vehicle Credit

The legislation also adds a new credit for previously-owned electric vehicles purchased from 1/1/2023 to 12/31/2032. The value of this credit is the lesser of $4,000 or 30% of the vehicle's sale price. Effective 1/1/2023, buyers will be able to transfer the credit to the dealer at the time of acquisition to offset a portion of the cost of the vehicle.

Qualifying used vehicles must meet the requirements set out for the new clean vehicle credit. The model year must be within two calendar years of the year of purchase. The vehicle must be purchased from a dealer for $25,000 or less. Lastly, the sale must be the first transfer of the vehicle after the 8/16/2022 date of enactment.

It is important to note, that this credit is not available for taxpayers who purchase a vehicle for resale, dependents of another taxpayer, or someone who has previously claimed this credit within three years of the sale date.

Similar to the new clean vehicle credit, there is also a modified gross adjusted income limit for this credit: $150,000 for a joint return or surviving spouse, $112,500 for head of household, and $75,000 for others. However, unlike the new clean vehicle credit, taxpayers may use the lesser of the current year or prior year modified adjusted gross income to qualify.

Excess Business Loss limitation Extension

Under prior legislation, taxpayers other than C corporations were limited on the amount of pass-through business losses they could deduct in a year. The annual limit is $500,000 for married filing joint filers, or $250,000 for all other filers. Any losses in excess of these limits were disallowed in the current year and carried forward to future tax years.

The current legislation extends this provision until 12/31/2028.

Miscellaneous Healthcare Related Provisions

In addition to the individual tax provisions above, the legislation has several healthcare related provisions that will impact qualifying individuals over the next few years. The first is the extension of the existing health insurance premium tax credits through 12/31/2025. To be eligible for these credits, a taxpayer must have acquired health insurance through one of the health insurance exchanges and typically needs to have income of 400% or less of the federal poverty line.

The legislation also includes several changes that will impact Medicare eligible taxpayers over the coming years. These changes include imposing a $35/month copay cap on insulin products starting in 2023, capping how much seniors spend on copays and coinsurance for drugs at $2,000 annually beginning in 2025, and limiting annual Medicare drug premium increases to no more than 6% through 2029. In addition, Medicare will now be able to negotiate pricing for up to 10 negotiation-eligible drugs with new prices taking effect in 2026. The number of drugs eligible to be negotiated will be increased to 20 starting in 2029.

Given the recent nature of this legislation, several of the provisions discussed above require the development of additional guidelines. SilverOak will continue to monitor these items as pertinent details become available. If you are interested in discussing these provisions further, or any other component of the Inflation Reduction Act, please contact your SilverOak Advisor or call 952-896-5700.