After years of pandemic-related issues plaguing the Internal Revenue Service (with some backlog issues still lingering), the 2023 tax filing season was a relatively quiet one, with the biggest news coming as the season drew to a close – the release of the Strategic Operating Plan that reveals how the agency will spend the nearly $80 billion allocated to it by the Inflation Reduction Act of 2022.

The generally quiet tax season also saw the release of green energy tax-related guidance, both for buildings and vehicles, as well as a new program for service industry workers to report tips and guidance on excise taxes for corporate stock buybacks.

### STRATEGIC OPERATING PLAN

The Strategic Operating Plan was released April 6, 2023, after missing the deadline for its release as outlined in the Inflation Reduction Act of 2022, but the delay was presumably due to the transition of leadership at the IRS, with Daniel Werfel officially sworn in on April 4, 2023, after being confirmed by the Senate on March 9, 2023.

The goal of the changes outlined in the Strategic Operating Plan is to “provide taxpayers with world-class customer service” and reduce the deficit by “hundreds of billions by pursuing tax evasion by wealthy individuals, big corporations, and complex partnerships,” said Deputy Secretary of the Treasury Wally Adeyemo.

The Strategic Operating Plan is organized around five key objectives:

- Dramatically improve services to help taxpayers meet their obligations and receive the tax incentives for which they are eligible.
“With Republicans taking control of the House ... and Democrats holding on to a slim majority in the Senate, significant tax legislation is not expected in the coming year.”

- Quickly resolve taxpayer issues when they arise.
- Focus expanded enforcement on taxpayers with complex tax filings and high-dollar noncompliance to address the tax gap.
- Deliver cutting-edge technology, data, and analytics to operate more effectively.
- Attract, retain, and empower a highly skilled, diverse workforce and develop a culture that is better equipped to deliver results for taxpayers.

The plan outlines a series of initiatives and projects aligned to each objective, including 42 key initiatives, 190 key projects, and more than 200 specific milestones designed to achieve the objectives set forth by the IRS.

The Strategic Operating Plan also includes targeted efforts to ensure fair tax law enforcement and compliance with existing laws. The plan focuses on “areas where compliance has eroded the most,” specifically compliance issues involving “wealthy individuals, complex partnerships, and large corporations,” said Werfel. The IRS will increase hiring efforts for experienced accountants and attorneys to ensure enforcement “at the top.” Werfel further noted that the IRS does not intend to increase the audit rate for small businesses or households making less than $400,000.

Finally, the Strategic Operating Plan utilizes Inflation Reduction Act funding to modernize the agency’s technology infrastructure to protect taxpayer data. In the first five years of the 10-year plan, the IRS aims to eliminate paper backlogs that have delayed taxpayer refunds by digitizing forms and returns when they are received and transitioning to fully digital correspondence processes.

LEGISLATIVE UPDATE

With Republicans taking control of the House of Representatives during the mid-term election cycle and Democrats holding on to a slim majority in the Senate, significant tax legislation is not expected in the coming year. Instead, look for more work to be done on oversight, especially in the House.

However, even if legislation is produced, the rules that legislators in the House have to follow could affect what legislation is able to accomplish.

The rules, which were adopted January 9, 2023, almost exclusively along party lines (only one Republican voted against and no Democrats voted in favor), contain two key provisions that could impact tax policy in at least the next two years. First is the need for a supermajority of lawmakers to vote in favor of a tax rate increase and the second is a replacement of the “pay as you go” rule (any increase in spending needs a mechanism to fund the increase) to a “cut as you go” rule, which means any increase in spending in one area must be offset by a cut of funding in another area.

A summary of the rules states that it “restores a requirement for a three-fifths supermajority vote on tax rate increases.” This is likely to have little impact as there likely will not be any proposals to increase taxes coming out of the GOP-led House, especially considering many Republicans signed a pledge to oppose increase taxes.

The second provision, cut as you go, requires that increases in mandatory spending programs, including programs such as Social Security, Medicare, veterans’ benefits and unemployment compensation, be offset by cuts to other mandatory spending programs.

“This means that the House cannot even pass increases to these programs that are fully paid for with new revenue, unless they also cut some other program in this category,” Joe Hughes, federal policy analyst at the Institute on Taxation and Economic Policy, noted in a blog on the rules.

This could make passage of enhancements to popular tax provisions more problematic. For example, the cut as you go rule “makes it harder to enhance ... policies like the Child Tax Credit (CTC) or Earned Income Tax Credit (EITC) because the refundable portions of the credits—the amount that can exceed the income tax a family would otherwise owe—are counted as mandatory spending under the budget scoring rules used by Congress,” Hughes writes, noting that any improvements would
require cuts to another essential program like Social Security or Medicare.

“Advocates and lawmakers hoping to restore the 2021 expansion, or otherwise improve the CTC or EITC, will now face an even tougher road ahead” due to the cut as you go rule, he states.

**GREEN ENERGY TAX CREDITS**

**Advanced Energy Project Program**

The IRS announced a program to allocate $10 billion of credits for qualified investments in eligible qualifying advanced energy projects (the Code Sec. 48C(e) program). At least $4 billion of these credits may be allocated only to projects located in certain energy communities.

The guidance announcing the program also:

- Defines key terms, including qualifying advanced energy project, specified advanced energy property, eligible property, the placed in service date, industrial facility, manufacturing facilities, and recycling facility;
- Describes the prevailing wage and apprenticeship requirements, along with remediation options; and
- Sets forth the program timeline and the steps the taxpayer must follow.

For Round 1 of the Code Sec. 48C(e) program, the application period begins on May 31, 2023. The IRS expects to allocate $4 billion in credits in this round, including $1.6 billion to projects in energy communities.

The taxpayer must submit a concept paper detailing the project by July 31, 2023. The taxpayer must also certify under penalties of perjury that it did not claim a credit under several other Code Sections for the same investment.

Within two years after the IRS accepts an allocation application, the taxpayer must submit evidence to the DOE to establish that it has met all requirements necessary to commence construction of the project. DOE then notifies the IRS, and the IRS certifies the project.

Taxpayers generally submit their papers through the Department of Energy (DOE) eXCHANGE portal at https://infrastructure-exchange.energy.gov/. The DOE must recommend and rank the project to the IRS, and have a reasonable expectation of its commercial viability.

The guidance also provides additional procedures for energy communities and the credit for progress expenditures.

For purposes of the minimum $4 billion allocation for projects in energy communities, the DOE will determine which projects are in energy community census tracts. Additional guidance is expected to provide a mapping tool that applicants for allocations may use to determine if their projects are in energy communities.

Finally, the guidance explains how taxpayers may elect to claim the credit for progress expenditures paid or incurred during the tax year for construction of a qualifying advanced energy project. The taxpayer cannot make the election before receiving its certification letter.

**Bonus Energy Credits for Energy Communities**

IRS guidance previews likely regulations governing energy communities for purposes of the bonus credits that are part of several energy-related credits. The IRS expects the regulations will apply to tax years ending after April 4, 2023.

The Inflation Reduction Act of 2022 added energy community provisions to the following credits:

- The Code Sec. 45 production tax credit for electricity produced from certain resources;
- The Code Sec. 45Y clean electricity production credit, a resource-neutral credit that largely replaces the Code Sec. 45 credit for property placed in service after 2024;
- The Code Sec. 48 business energy investment credit for investments in property that produces electricity from certain resources; and
- The Code Sec. 48E clean energy investment credit, a resource-neutral credit that largely replaces the Code Sec. 48 credit for property placed in service after 2024.
The credit rate for these credits may be increased for qualified facilities, energy projects or energy storage technologies that are placed in service in energy communities. There are three types of energy communities:

- **Brownfield category**—a site where development or reuse may be complicated by the presence of a hazardous substance, pollutant or contaminant, or certain mine-scarred land.
- **Statistical area category**—metropolitan statistical areas (MSAs) or non-MSAs with certain levels of employment or local tax revenues related to fossil fuels, and unemployment rates at or above the national average.
- **Coal closure category**—a census tract (or a directly adjoining tract) in which a coal mine closed after 1999, or a coal-fired electric generating plant was retired after 2009.

The guidance provides a safe harbor for identifying brownfield sites, and detailed definitions for the statistical area and coal closure categories. In addition, for purposes of the statistical area category, the guidance lists MSAs and non-MSAs, and those that satisfy the fossil fuel employment threshold are identified, with expected updates provided in May of future years.

Finally, census tracts that are in the coal closure category are also identified. The production credits require a qualified facility to be located in an energy community, and the investment credits require an energy project, qualified facility or energy storage technology to be placed in service in an energy community. For the production credits, this determination is made for each tax year during the 10-year credit period. For the investment credits, this determination is made on the date the property is placed in service.

However, for qualified property in a location that is an energy community as of the beginning of construction (BOC) date, the location will be considered an energy community for the duration of the credit period. Property is located in an energy community:

- If at least 50 percent of its nameplate capacity is in an energy community (the nameplate capacity test); or
- If it has no nameplate capacity, at least 50 percent of its square footage is in an energy community (the footprint test).

### Low-Income Communities Bonus Credit

The IRS established the program to allocate environmental justice solar and wind capacity limitation (Capacity Limitation) to qualified solar and wind facilities eligible for the Low-Income Communities Bonus Credit Program component of the energy investment credit. The IRS also provided:

- Initial guidance regarding the overall program design,
- The application process, and
- Additional criteria that will be considered in making the allocations.

After the 2023 allocation process begins, the Treasury Department and IRS will monitor and assess whether to implement any modifications to the Low-Income Communities Bonus Credit Program for calendar year 2024 allocations of Capacity Limitation.

The program establishes four facilities categories and the capacity limitation for each:

1. Facilities located in low-income communities will have a capacity limitation of 700 megawatts;
2. Facilities located on Indian land will have a capacity limitation of 200 megawatts;
3. Facilities that are part of a qualified low-income residential building project have a capacity limitation of 200 megawatts; and
4. Facilities that are part of a qualified low-income economic benefit project have a capacity limitation of 700 megawatts.

The IRS anticipates applications will be accepted for Category 3 and Category 4 facilities in the third quarter of 2023. Applications for Category 1 and Category 2 facilities will be accepted thereafter. The IRS will issue additional guidance regarding the application process and facility eligibility.
The program will also incorporate additional criteria in determining how to allocate the Capacity Limitation reserved for each facility category among eligible applicants. These may include a focus on facilities that are owned or developed by community-based organizations and mission-driven entities, have an impact on encouraging new market participants, provide substantial benefits to low-income communities and individuals marginalized from economic opportunities, and have a higher degree of commercial readiness.

Finally, only the owner of a facility may apply for an allocation of Capacity Limitation. Facilities placed in service prior to being awarded an allocation of Capacity Limitation are not eligible to receive an allocation. The Department of Energy (DOE) will provide administration services for the Low-Income Communities Bonus Credit Program. An allocation of an amount of capacity limitation is not a determination that the facility will qualify for the energy investment credit or the increase in the credit under the Low-Income Communities Bonus Credit Program.

Battery Requirements for Clean Vehicle Credit

Proposed regulations spell out the critical mineral and battery component requirements of the new clean vehicle credit, while also clarifying several other components of the credit. The proposed regulations, along with modified Frequently Asked Questions on the IRS website, largely adopt previous IRS guidance, including Rev. Proc. 2022-42, Notice 2023-1, and Notice 2023-16. Similarly, the critical minerals and battery component regs largely adopt the White Paper the Treasury Department released last December. The regulations are generally proposed to apply to new clean vehicles placed in service after April 17, the date they are scheduled to be published in the Federal Register.

However, the proposed regulations also:
• Detail the income and price limits on the credit,
• Prohibit multiple taxpayers from dividing the credit for a single vehicle, and
• Coordinate the credit with other credits.

Critical Minerals Requirements: For purposes of the $3,750 credit for a qualified vehicle that satisfies the critical minerals requirement, the proposed regulations provide a three-step process for determining the percentage of the value of the applicable critical minerals in a battery:
• Determine the procurement chain for each critical mineral.
• Identify qualifying critical minerals.
• Calculate qualifying critical mineral content.

The proposed regulations define relevant terms, including “procurement chain,” “critical minerals,” “critical mineral content,” “extraction,” “processing,” “constituent materials,” “recycling,” and “value added.”

For vehicles placed in service in 2023 and 2024, the proposed regulations consider a critical mineral to meet the test if at least 50 percent of the value added by extracting, processing or recycling the mineral is due to extraction, processing or recycling in the U.S. or a country with which the U.S. has a free trade agreement in effect. The proposed regulations identify the following countries as ones with a free trade agreement in effect with the U.S.: Australia, Bahrain, Canada, Chile, Colombia, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Israel, Jordan, Korea, Mexico, Morocco, Nicaragua, Oman, Panama, Peru, and Singapore. The regulations also propose criteria for identifying additional countries, such as the factors that are part of the Critical Minerals Agreement (CMA) the U.S. recently entered into with Japan.

Battery Component Requirement: For purposes of the $3,750 credit for a qualified vehicle that satisfies the battery components requirement, the proposed regulations provide a four-step process for determining the percentage of the value of the battery components in a battery:
• Identify components that are manufactured or assembled in North America.
• Determine the incremental value of each battery component and North American battery component.
• Determine the total incremental value of battery components.
• Calculate the qualifying battery component.
MAGI Limit: The credit does not apply if the taxpayer’s modified adjusted gross income (MAGI) for the credit year or, if less, the previous year exceeds a limit based on filing status. The proposed regulations clarify that if the taxpayer’s filing status changes during this two-year period, this test applies the MAGI limit for each year based on the taxpayer’s filing status for that year. The proposed regulations also clarify that the MAGI limit does not apply to a corporation or any other taxpayer that is not an individual for which AGI is computed under Code Sec. 62.

MSRP Limits: A vehicle does not qualify for the credit if the manufacturer’s suggested retail price (MSRP) exceeds $80,000 for a van, sport utility vehicle (SUV), or pickup truck; or $55,000 for any other vehicle. The proposed regulations adopt the vehicle classification system the IRS announced in Notice 2023-16. This is the vehicle classification that appears on the vehicle label and on the website FuelEconomy.gov. The regulations also provide a more detailed definition of “MSRP” using information reported on the label affixed to the vehicle’s windshield or side window.

Vehicle with Multiple Owners: The proposed regulations generally prohibit any allocation or proration of the credit if multiple taxpayers place a vehicle in service. However, a partnership or S corporation that places a vehicle in service may allocate the credit among its partners or shareholders. The MAGI limits on the credit apply separately to each individual partner or shareholder. The seller’s report for the vehicle lists the entity’s name and TIN.

Final Assembly in North America: To qualify for the credit, the final assembly of a new clean vehicle must occur in North America. The proposed regulations reiterate earlier guidance on this requirement, but they also provide more detailed definitions of “final assembly” and “North America.” Taxpayers may rely on the vehicle’s plant of manufacture as reported in the vehicle identification number (VIN), or the final assembly point reported on the label affixed to the vehicle. Taxpayers may also continue to rely on the information in the “VIN decoder sites.”

Coordination with Other Credits: While the new vehicle credit is generally a nonrefundable personal credit, the credit for a depreciable vehicle is treated as part of the general business credit. If the taxpayer’s business use of a qualified vehicle is less than 50 percent of its total use, the proposed regulations require the taxpayer to apportion the credit. Only the portion of the credit that corresponds to the percentage of the taxpayer’s business use of the vehicle is part of the general business credit; the rest of the credit remains a nonrefundable personal credit.

The proposed regulations clarify that when the new clean vehicle credit is allowed for a particular vehicle, a subsequent buyer in a later tax year may still claim the used clean vehicle credit. However, a subsequent buyer cannot claim the commercial clean vehicle credit.

OTHER DEVELOPMENTS

Service Industry Tip Reporting Program

The IRS issued a notice which contains a proposed revenue procedure that would establish the Service Industry Tip Compliance Agreement (SITCA) program, a voluntary tip reporting program between the IRS and employers in various service industries. The SITCA program is designed to take advantage of advancements in point-of-sale, time, and attendance systems and electronic payment settlement methods to improve tip reporting compliance. The proposed program would also decrease taxpayer and IRS administrative burdens and provide more transparency and certainty to taxpayers.

The proposed program includes the following features:

• Employer compliance monitored based on actual annual tip revenue and charge tip data from an employer’s point-of-sale system, and allowance for adjustments in tipping practices from year to year;

• Participating employers demonstrate compliance with the program requirements by submitting an annual report after the close of the calendar year, which reduces the need for compliance reviews by the IRS;
• Participating employers receive protection from liability under the rules that define tips as part of an employee’s pay for calendar years in which they remain compliant with program requirements; and

• Participating employers have flexibility to implement employee tip reporting policies that are best suited for their employees and their business model in accordance with the section of the tax law that requires employees to report tips to their employers.

The IRS is continuing to explore opportunities within the gaming industry and this program does not affect the existing Gaming Industry Tip Compliance Agreement (GITCA) program. Existing agreements would remain in effect until the earlier of: the employer’s acceptance into the SITCA program; an IRS determination that the employer is noncompliant with the terms of their TRDA, TRAC, or EmTRAC agreement; or the end of the first full calendar year after the final revenue procedure is published in the Internal Revenue Bulletin.

Corporate Stock Repurchase Excise Tax

The IRS provided guidance announcing that they intend to issue proposed regulations to address the application of the new one-percent corporate stock repurchase excise tax under Code Sec. 4501, which was added by the Inflation Reduction Act of 2022.

Beginning in 2023, a publicly traded U.S. corporation is subject to a one-percent excise tax on the value of its stock that the corporation repurchases during the tax year, effective for stock repurchases made after December 31, 2022. Repurchases include stock redemptions, as well as economically similar transactions as determined by the Treasury Secretary. Specified exceptions to the tax may be applicable.

The interim guidance is intended to clarify excise tax calculation, and the application of Code Sec. 4501 to certain transactions and other events occurring before the proposed regulations are issued.

Among other things, the interim guidance addresses the $1 million de minimis exception; the stock repurchase excise tax base; redemptions and economically similar transactions; acquisitions by specified affiliates, applicable specified affiliates, or covered surrogate foreign corporations; timing and fair market value of repurchased stock; statutory exceptions; and a netting rule. The guidance also includes illustrative examples.

The proposed regulations are anticipated to provide that the stock repurchase excise tax must be reported on IRS Form 720, Quarterly Federal Excise Tax Return. To facilitate the tax computation, the IRS also intends to issue an additional form that taxpayers will be required to attach to Form 720.

Although Form 720 is filed quarterly, the Treasury and IRS expect the proposed regulations to provide that the stock repurchase tax will be reported once per tax year, on the Form 720 that is due for the first full quarter after the close of the taxpayer’s tax year.

The proposed regulations are anticipated to provide that rules consistent with those in the guidance will generally apply to repurchases of stock of a covered corporation made after December 31, 2022, and to issuances of stock made during a tax year ending after December 31, 2022. Rules consistent with those in the guidance on purchases funded by applicable specified affiliates will apply to repurchases and acquisitions of stock made after December 31, 2022, that are funded on or after the date the guidance is released to the public.

Until the proposed regulations are issued, taxpayers can rely on the rules in the guidance.
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