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In this article, Unell and Marencik examine a potential and overlooked consequence of the Build Back Better Act for corporate taxpayers continuing to carry forward minimum tax credits under the old alternative minimum tax regime.

On November 19, 2021, the Build Back Better Act (BBBA) (H.R. 5376) passed in the House by a vote of 220 to 213. The Senate Finance Committee then released a draft of its legislation on December 11. But on December 19, Sen. Joe Manchin III, D-W.Va., announced that he would not support the legislation, which, given the composition of the current Congress, makes it highly unlikely the bill will pass in its current form. While some parts of the BBBA may make it through Congress, as of now it is not clear which (if any) will make it. We therefore are taking advantage of the delay in the legislative process to point out a rather punitive but potentially unintended consequence of one proposal in the hopes that the next version may be drafted to avoid this result.

Among many other things, the BBBA would have introduced a new alternative minimum tax regime that would have imposed a 15 percent corporate alternative minimum tax on the adjusted financial statement income of some large corporations.[1] This new AMT attracted a lot of attention for what it intended to accomplish, but one element of the proposed legislation had been generally overlooked: the potential effect of the new AMT on corporate taxpayers continuing to carry forward minimum tax credits under the old AMT regime.

It is not entirely surprising that these taxpayers were overlooked. The only corporate taxpayers continuing to carry forward AMT credits under the old AMT regime are those that were overlooked in 2017, when Congress acted to phase out the corporate AMT and make (nearly) all corporate AMT credits refundable by 2021 — and overlooked again in 2020, when Congress accelerated the time frame to refund (nearly) all corporate AMT credits. The failure to account for these taxpayers in 2017 and 2020 was unfortunate, but in those years that failure just meant they were not eligible to accelerate the use of their credits. Failure to account for these taxpayers in the BBBA could have wiped out their credits entirely.

Carry Forward of 'Old' Corporate AMT Credits

On December 20, 2017, the House passed the Tax Cuts and Jobs Act, which was signed into law by then-President Trump on December 22 of that year. Among other things, the TCJA repealed the AMT historically imposed on corporations.[2] The TCJA also modified the AMT credit refund provisions to treat a corporation's tentative minimum tax liability as zero.[3] As a result, AMT credits, available to offset the excess of regular tax liability over tentative minimum tax, became eligible to fully offset regular tax.

[1] H.R. 5376, section 138101(a).

[2] Section 55(a), as amended by the TCJA.

[3] Section 53(e), as amended by the TCJA. Under prior law, AMT credits were permitted as an offset to regular tax to the extent that regular tax was not reduced below tentative minimum tax. The TCJA effectively removed the tentative minimum tax limiter and, in doing so, increased the extent of the regular tax offset.

The TCJA also modified section 53(e) to permit a portion of the a corporation's AMT credit carryforward to be a refundable credit under subpart C.[4] Initially, for tax years beginning in 2018, 2019, and 2020, the AMT refundable credit amount was equal to 50 percent of the excess of the AMT credit carried into the year (as determined under section 53(b)) less the AMT credit allowed as an offset to regular tax in the current year under section 53(a).[5] The AMT refundable credit amount increased to 100 percent of that excess for tax years beginning in 2021.[6] The expressed intent of this modification was to permit a corporation previously subject to the AMT to recover its AMT credit carryforward by the end of its last tax year beginning in 2021.[7] Despite the legislative intent as set forth in the conference committee's joint explanation of the AMT credit provisions implemented by the TCJA, many practitioners believe that an interaction between the AMT refundable credit rules and section 383 prevented some corporations from recovering their full AMT credits through the refund mechanism.[8]

Section 383 generally applies to corporations that have undergone an ownership change as defined in section 382. Under section 383, credit carryovers from years before an ownership change can offset tax liability only to the extent of a corporation's available limitation under section 382, an amount generally computed by regard to the corporation's equity value at the time of the ownership change.[9] Reg. section 1.383-1(d) provides that "the amount of *regular tax liability* of a new loss corporation for any post-change year that may be *offset* by pre-change credits shall not exceed the amount of the section 383 credit limitation for the post-change year" (emphasis added).[10] And in administrative guidance the IRS has acknowledged that the language of reg. section 1.383-1(d) makes clear that section 383 applies to limit the use of credits that offset regular tax liability but has no basis for limiting credits that give rise to a refund.[11]

Under this analysis, it would seem that section 383 should not have limited a taxpayer's ability to receive the benefit of its AMT credits through refunds regardless of whether the credits were subject to a section 383 limitation, and in fact some taxpayers subject to restrictive section 383 limitations were able to get their full AMT credits refunded. However, an odd quirk in the refund mechanics had the unexpected result of denying the refund to those taxpayers whose regular tax liability for the years in question exceeded the amount of credit that could have been used to offset that liability as a result of section 383.

Generally, refundable credits are those allowable under subpart C of Part IV of subchapter A of chapter 1 of the code. Section 6401(b)(1) provides:

> If the amount allowable as credits under subpart C of part IV of subchapter A of chapter 1 (relating to refundable credits) exceeds *the tax imposed by subtitle A* (reduced by the credits allowable under subparts A, B, D, and G of such part IV), the amount of such excess shall be

[4] *Id.*

[5] *Id.* The limitation under section 53(c) was also increased by the AMT refundable credit amount for that year. Accordingly, the AMT credits carried into the year under section 53(b) would be subject to an elevated section 53(c) limitation and be allowed as an offset to tax under section 53(a). A portion of the remaining section 53(b) carryforward was then treated as a refundable subpart C credit.

[6] *Id.* The Coronavirus Aid, Relief, and Economic Security Act later increased the AMT refundable credit amount to 100 percent for tax years beginning in 2019 and eliminated the applicability of the refund provisions to tax years beginning in 2020 and 2021.

[7] *See* Joint Committee on Taxation, "Description of the Chairman's Mark of the 'Tax Cuts and Jobs Act,'" JCX-51-17, at 152 (Nov. 9, 2017) (providing that "the full amount of the minimum tax credit will be allowed in taxable years beginning before 2022").

[8] The discussion of the AMT credit refund provisions is an abbreviated discussion of the relevant statutory provisions and their application. For a more detailed analysis of those provisions, refer to Mark R. Hoffenberg and Stephen M. Marencik, "Are AMT Credit Refunds Subject to Limitation?" *Tax Notes Federal*, Feb. 26, 2018, p. 1177.

[9] Under section 383 and the regulations thereunder, some conforming adjustments to the limitation under section 382 are required. *See* reg. section 1.383-1(e)(2).

[10] Reg. section 1.383-1(d)(1).

[11] *See* ILM 201126029. This also appears consistent with the loss trafficking policy of sections 382 and 383. Very generally, those limitations are intended to prevent the acquisition of stock of a corporation with losses or other tax attributes (that is, a loss corporation) in order to monetize those attributes when those attributes could not otherwise be monetized by the loss corporation and its shareholders on account of insufficient taxable income or tax liability. For a refundable credit, that policy is not present because, due to the refundable nature of the credit, the attribute could have been monetized by the loss corporation as a refund irrespective of it having standalone tax liability.

considered an overpayment. [Emphasis added.]

Credits actually allowable under subpart C of Part IV of subchapter A of chapter 1 of the code are generally not subject to section 383, presumably for the simple reason that there is limited ability to traffic in those credits. Section 53(e)(3) treated some amounts of a corporation's AMT credit carryovers as allowable under that subpart, and therefore governed by section 6401(b)(1). But the amount of credit treated as an overpayment is only the excess of the credit over the regular tax liability of the corporation. To the extent that the corporation has residual regular tax liability that cannot be offset with credits because of a section 383 limitation, those credits are also not treated as an overpayment, and therefore do not give rise to a cash refund.

The quirk in the statute is best illustrated by the following example.

Example 1: Assume Corp. X paid AMT of $100 in year 1, a pre-TCJA year. On the first day of year 2, a year following enactment of the TCJA in which the refund percentage is 50 percent, Corp. X experienced an ownership change within the meaning of section 382. The ownership change resulted in an annual section 383 limitation of $10. In year 2 Corp. X has a regular tax liability of $40. Assume Corp. X has no other tax attributes.

Corp. X carried $100 of AMT credits into year 2. Under section 53(e), the AMT refundable credit amount in year 2 would be $45, which is equal to 50 percent of $90 (the excess of the $100 of AMT credits carried into the year less the amount of the AMT credit available to offset regular tax liability in the current year on account of section 383). Because of the $10 limitation under section 383, Corp. X's regular tax liability of $40 would be reduced by $10 to $30. Under sections 6401 and 6402, only the excess of the refundable credit ($45) over Corp. X's regular tax liability reduced by nonrefundable credits ($30) is treated as an overpayment of tax. Consequently, Corp. X would be entitled to a refund of only $15 and would continue to carry forward AMT credits of $75 into year 3.

As a result of the refund mechanics, the only factor that really came into play in determining which corporations could not fully recover their AMT credits was the corporations' regular tax liability in the last year of the refund period. Corporations generating higher regular tax liability could recover less of their AMT credits. This result has no obvious policy justification.[12]

Example 2: Assume the same facts as in Example 1, except that the year is now year 3, which is the tax year beginning in 2019, and a year following enactment of the Coronavirus Aid, Relief, and Economic Security Act. Also assume that Corp. X generates regular tax liability of $200, or alternatively $0.

In the situation in which Corp. X generates $200 of regular tax, Corp. X's AMT refundable credit amount would be $65, which is equal to 100 percent of the excess of the AMT credit carried into the year less the $10 amount available as an offset to regular tax. However, because the AMT refundable credit amount of $65 does not exceed the residual regular tax liability of $190, Corp. X would be entitled to no refund and would carry forward an AMT credit of $65 into year 4.

Alternatively, in the situation in which Corp. X generates $0 of regular tax, Corp. X's AMT refundable credit amount would be $75, which is equal to 100 percent of the AMT credit carried into the year. Because the AMT refundable credit amount of $75 would exceed the residual regular tax liability of $0, Corp. X would be entitled to a refund of $75 and would carry forward no AMT credit into year 4.

Effect of BBBA Proposals

Although the intent may have been to eliminate corporate AMT credit carryovers by the time section 53(e) was sunset, the mechanics discussed above resulted in some corporate taxpayers continuing to carry forward AMT

[12] Note that taxpayers could be subject to this result even for AMT credits directly attributable to post-ownership-change losses. In particular, if a taxpayer had paid tax in pre-ownership-change periods and then generated losses in a post-ownership-change year that were carried back to offset pre-ownership-change tax liability, that carryback could result in some of what was previously regular tax becoming characterized as AMT because of differential computations of allowable carrybacks for regular tax and AMT purposes. The taxpayer's post-change net operating loss would have resulted in a partial refund of prior tax and a partial conversion of tax paid from regular tax to AMT, and a corresponding AMT credit. That credit, arising from tax paid in a pre-change year, appears subject to section 383 limitation even though the losses that gave rise to it were post-change losses. In this regard, the NOL carryback provisions under the CARES Act may have increased the number of corporations with AMT credit carryforwards and exacerbated this unintended effect of the AMT credit refund mechanism.

credits. Because the TCJA left intact the underlying rule that AMT credits could be used to the extent of the excess of regular tax liability over tentative minimum tax liability, corporate taxpayers left out of the refund regime could at least look forward to taking into account their AMT credits over time as an offset to regular tax, to the extent their section 383 limitations allowed. But if the BBBA were to pass as proposed or if subsequent legislation adopts the new alternative minimum tax regime and new AMT credit provisions in their current form, even this cold comfort will be stripped away — at least from the most profitable of corporations.

The BBBA would have imposed a new 15 percent corporate minimum tax (that is, the new AMT) on some "applicable corporations." Under the new AMT, whether a corporation is an applicable corporation depends on specified book income metrics,[13] and there is some potential for corporations to move from being applicable to no longer being applicable. It would also permit a credit to corporations that paid new AMT in prior years for years in which those corporations are not paying new AMT (that credit, a "new AMT credit").

The basic mechanism for the new AMT credit is the same as the basic mechanism for AMT credits under pre-TCJA law, mostly because the BBBA would leave the majority of section 53 intact. However, the BBBA did propose to make one critical change to section 53. Section 138101(e)(1) of the BBBA provided:

> Section 53(e) is amended to read as follows:
>
> (e) APPLICATION TO APPLICABLE CORPORATIONS. — In the case of an applicable corporation — (1) subsection (b)(1) shall be applied by substituting *"the net minimum tax for all prior taxable years beginning after 2022" for "the adjusted net minimum tax imposed for all prior taxable years beginning after 1986."*[14] [Emphasis added.]

The effect of this provision would have been to define minimum tax credit carryovers for applicable corporations by reference only to post-2022 AMT (that is, the new AMT). As a result, any pre-TCJA AMT credits of an applicable corporation that would have continued to be carried forward as a result of the phenomenon described above would be trapped with no potential to be used as an offset to regular tax liability under section 53(a) to the extent that the corporation remained an applicable corporation.[15] Conversely, for corporations other than applicable corporations, the BBBA did not propose changes to section 53(a) or (b). It therefore appears that corporations other than applicable corporations could have continued to carry forward AMT credits generated before the TCJA under section 53(b) and use those credits as an offset to tax under section 53(a). The net effect of this statutory change is best illustrated by the following example.

Example 3: Assume the same facts as in Example 1, except that the year is now year 6, which is a year following enactment of the BBBA in its proposed form. Also assume that, but for new section 53(e) (revising section 53(b)), Corp. X would continue to carry forward AMT credits of $30.

If Corp. X is an "applicable corporation" as defined in section 138101(a) of the BBBA, Corp. X's AMT credit carryforwards under section 53(b) would be zero, as its AMT credits would only include credits generated on account of net minimum tax paid for all years beginning after 2023 (that is, the new AMT). Accordingly, no AMT credits generated before the TCJA would be available to Corp. X as an offset to regular tax under section 53(a).

[13] Very generally, corporations reporting at least $1 billion average adjusted pretax net income on their consolidated financial statements for any consecutive three-year period would be applicable corporations subject to the new AMT.

[14] Section 138101(e)(2) of the BBBA would make some other conforming adjustments, and the amendments under section 138101(e) of the BBBA would be applicable to tax years beginning after December 31, 2022.

[15] Note that for purposes of section 53(a), the AMT credit for any tax year is the amount defined in section 53(b); thus, the section 53(a) amount would be determined without regard to any AMT credits generated under pre-2022 law in this instance.

Conversely, if Corp. X is not an "applicable corporation" as defined in section 138101(a) of the BBBA, Corp. X's AMT credit carryforwards under section 53(b) would be $30, as its AMT credits would continue to include credits generated on account of net minimum tax paid in years before 2022. Accordingly, $10 (that is, equal to the section 383 limitation) of the AMT credits generated before the TCJA would be available to Corp. X as an offset to regular tax under section 53(a) in year 6.

Conclusion

It is not at all clear what the drafters of the BBBA were trying to accomplish with the new proposed section 53(e). The proposal suggests some awareness that there exist corporate taxpayers that continue to carry forward pre-TCJA AMT credits. If not, why add this rule at all? But we can think of no compelling policy reason to have excluded those taxpayers from the original refund provisions of the TCJA and the CARES Act, and even less reason to further curtail (or effectively eliminate) any residual benefit under the BBBA. Further, the degree of arbitrariness is disturbing — both the relative arbitrariness in which only profitable corporations were not able to fully benefit from the refund in the first instance and the decision to effectively eliminate ongoing carry forward of remaining AMT credits only for applicable corporations. If a subsequent iteration of the BBBA does include a new alternative minimum tax, then further consideration ought to be given to the mechanics that effectuate any corresponding credit and whether and how the mechanics should be harmonized with current section 53 to permit the use of old AMT credits that continue to exist under current law. Or perhaps even to eliminate those credits by explicitly permitting their refund notwithstanding section 383.[16] ■

[16] The information in this article is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser. This article represents the views of the author(s) only and does not necessarily represent the views or professional advice of KPMG LLP.