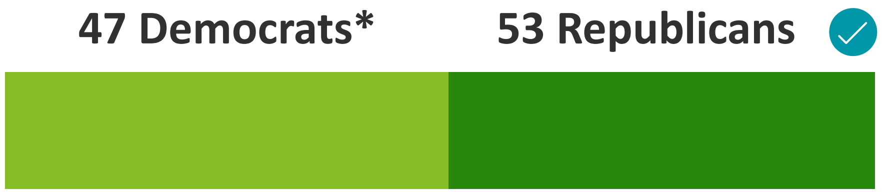
Deloitte.

The Post-Election Tax Policy Landscape: A Washington Update

January 15, 2024

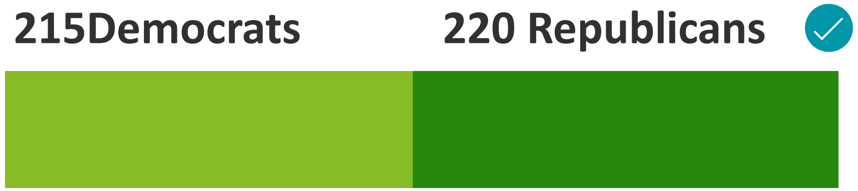
119 Congress: Initial observations

US SENATE



*Includes 2 Independents who caucus with Democrats

US HOUSE



Possible Election Impacts

- Republicans gain control of the Senate, but the **filibuster is expected to remain** in place
- Republicans retain **control of the House**, but with a razor-thin majority
- President-elect Trump can advance some policy priorities through **executive actions and regulatory authority**, including certain proposals related to energy, tariffs, and deregulation

2025: Taxes Take Center Stage

House approved bipartisan tax deal in early 2024

What does the future hold for these proposals?

BUSINESS INCENTIVES

- Delay R&D expense amortization (Sec. 174)
- Delay stricter limitation on business interest expensing (Sec. 163(j))
- Extend full expensing
- All retroactive through 2025

FAMILY INCENTIVES

- Index child tax credit and expand for 2023–2025

LOW–INCOME HOUSING TAX CREDIT

- Increase ceiling for state LIHTC
- Temporarily lower 50% bond–financing threshold

INTERNATIONAL BENEFITS

- Create US–Taiwan taax agreement

ADDITIONAL BENEFITS

- Increase reporting threshold for certain 1099s to $1k, from $600
- Tax relief for disaster–impacted communities

REVENUE RAISERS

- Hasten final deadline for ERTC claims to 1/31/24
- Extend statute of limitations on ERTC claims assessments
- Expand penalties for fraudulent ERTC claims

Trump's 2024 campaign continues to focus on his America First agenda

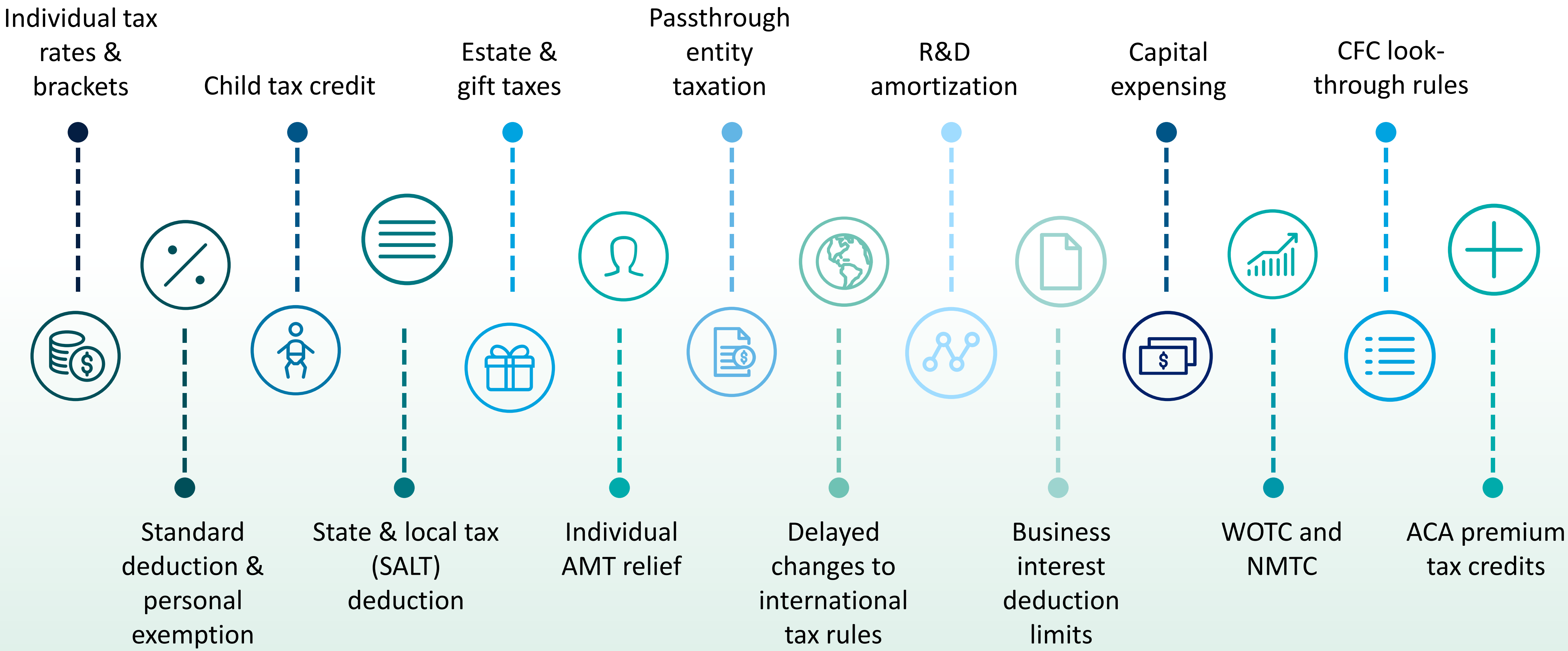
The former president would like to cut corporate taxes for domestic manufacturers

Specific tax and trade policy proposals President Trump campaigned on:

- Extend individual and business tax changes from TCJA that are due to sunset
- Impose tariffs of 10-20% on most imported goods, 60%+ on imports from China
- Create a new tax credit for family care givers
- Restore R&D expensing and 100% bonus depreciation
- Allow deduction for interest paid on automobile loans (for domestic vehicles only)
- Allow a deduction (retroactive) for costs paid by individuals to install power generators
- Ensure state and local taxes (SALT) are fully deductible for individuals
- Provide a tax deduction for the "major costs" associated with newborn babies
- Eliminate income taxes on overtime pay
- Eliminate income taxes on tips
- Eliminate income taxes on Social Security benefits
- Lower the corporate income tax rate to 15% for companies that make their products in America

Governing 2025 – Taxes will take center stage

The interactions and tradeoffs in the TCJA cliff negotiations will open with key provisions expiring at the end of 2025…



Pillar Two: Political dynamics of U.S. implementation

Expect the GOP to continue pushing back on global tax agreement

- Both Republicans and Democrats have raised concerns that P2 provides for more favorable treatment of refundable tax credits over the nonrefundable credits more prevalent in the U.S.
    - *E.g.,* the UK's refundable R&D tax credit is treated as income, while the U.S.' nonrefundable version is treated as a reduction in tax payments that can drop a company's effective tax rate < 15% and trigger a top-up tax

- House GOP legislative efforts include:
    - Calling for a policy rider as part of the FY2024 appropriations process that would prohibit US funding for the OECD
    - Imposing retaliatory taxes – subject to annual increases – on the US income of foreign entities and individuals from countries implementing a UTPR or similar measure
    - Tightening the U.S. base erosion and anti-avoidance tax (BEAT) rules for companies based in jurisdictions that impose a UTPR or other exterritorial tax on U.S. multinationals

- Impact of a President-elect Trump White House going forward:
    - Will other OECD countries "pause" collecting tax
    - Are other negotiating tools like tariffs on the table

IRS strategic operating plan, updated

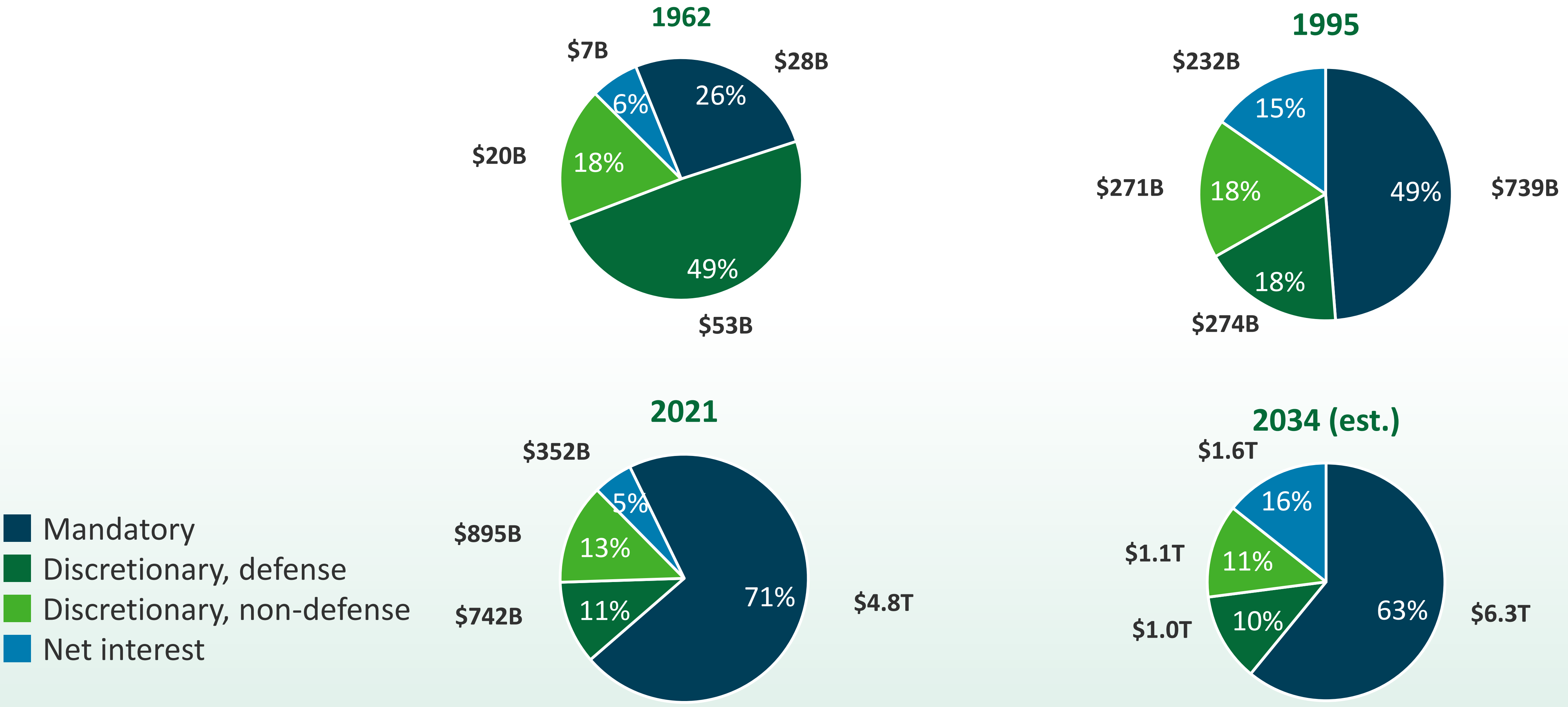
- The Inflation Reduction Act provided the Internal Revenue Service with about **$80B in additional appropriations** over 10 years, with about **$20B then rescinded** in March 2023 to cover other spending priorities
- An updated strategic plan released May 2 lays out the agency's plans to enhance enforcement and compliance activities, modernize its foundational technology, and improve tools available to IRS employees assisting taxpayers
- More than half of the total amount is allocated to enforcement, with a **focus on large corporate returns, complex passthrough entities, and high-net-worth individuals**, including plans to:
  - Nearly triple the audit rates on large corporations with assets greater than $250M to 22.6% in tax year 2026, up from 8.8% in tax year 2019
  - Increase audit rates by nearly 10-fold on large, complex partnerships with assets greater than $10M, going from 0.1% in 2019 to 1% in tax year 2026
  - Increase audit rates by more than 50% on wealthy individual taxpayers with total positive income greater than $10M, with audit rates going from an 11% coverage rate in 2019 to 16.5% in tax year 2026
- The IRS looks to **build its workforce** to 102,500 full-time equivalent employees by FY2029, up from roughly 83,000
- The plan makes the distinction that **no funds are to be used to increase the audit share of small businesses or households earning less than $400k** relative to historic levels, but expect continued political debate over allocation of funds to the IRS

Source: *IRA Strategic Operating Plan Annual Update*, Internal Revenue Service, May 2, 2024

The Fiscal Reality Facing our Elected Leaders

Mandatory spending and debt service is taking over the budget

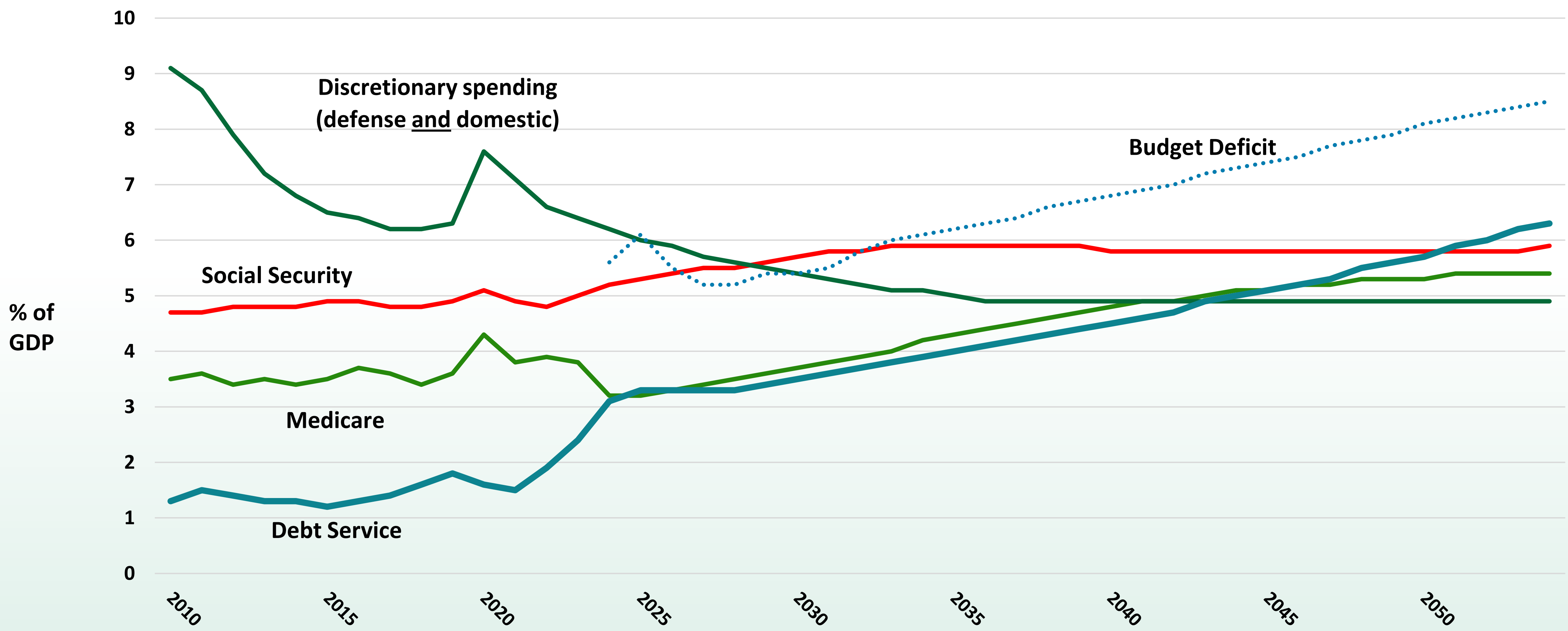
Without addressing entitlements, Congress will have less "discretion" over the nation's spending



Sources: Congressional Budget Office, *The Budget and Economic Outlook: 2024 to 2034* (Feb 2024) and accompanying historical data

Debt service costs on track to become the government's largest expenditure

Net interest costs expected to increase over the next decade



Sources: Congressional Budget Office, *The Long-Term Budget Outlook: 2024 to 2054* (March 2024) and accompanying historical data

Budget Reconciliation: The Process Driving Tax Policy

Reconciliation

A process that allows Senate passage of certain legislation with a simple majority.

Step 1:
Congress passes a budget resolution with reconciliation instructions

Step 2:
House and Senate committees report legislation

Step 3:
Senate conducts a Byrd Bath with the parliamentarian

Step 4:
House and Senate pass the identical bill

Step 5:
President signs bill into law

Expedited Senate procedures

- The motion to proceed is not debatable (i.e., it **cannot be filibustered**)
- Debate on the bill is limited to 20 hours
- All amendments must be germane
- The **final bill can pass with a simple majority**

Key Byrd rules

- **Every provision must change outlays or revenues**
- The **change cannot be incidental**
- The bill cannot increase the **deficit** in any fiscal year outside the budget window
- The bill cannot make changes to Social Security

Examples of past reconciliation bills

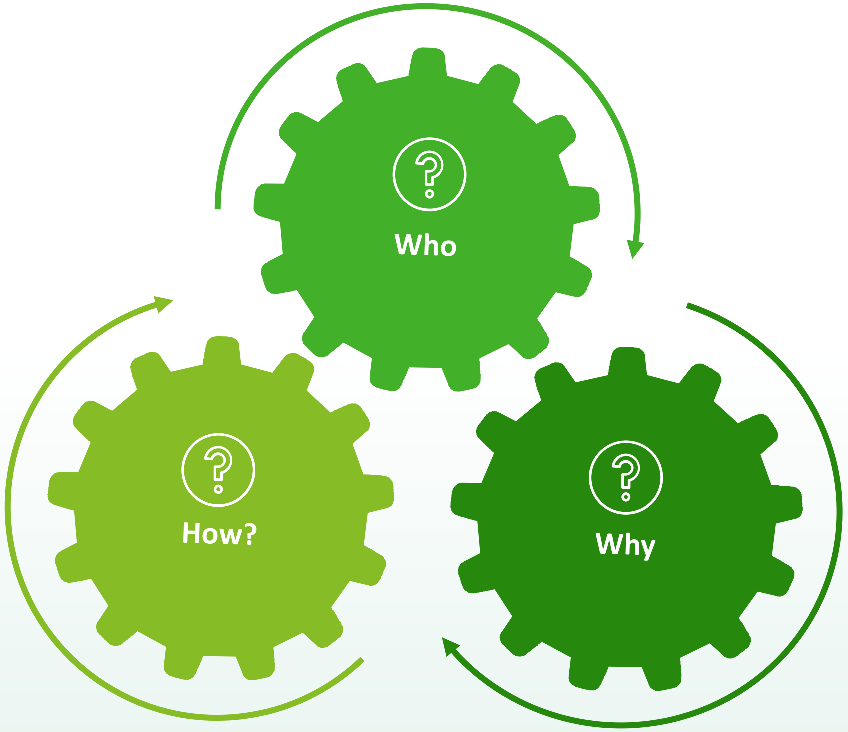
- 1996 Personal Responsibility and Work Opportunity Act
- 2001 Economic Growth and Tax Relief Reconciliation Act
- 2003 Jobs and Growth Tax Relief Act
- 2010 Health Care and Education Act
- 2017 Tax Cuts and Jobs Act
- 2021 American Rescue Plan Act
- 2022 Inflation Reduction Act

Who decides “the number”?

Members of the House and Senate (with input from the President)

How do you define “the number”?

The gross amount of additions to the deficit allowed under budget reconciliation



Why does “the number” matter?

Absent a large surprise, “the number” is going to be less than the ten-year revenue loss of extending expiring provisions of TCJA and the new policy proposals Donald Trump outlined on the campaign trail

What happens if “the number” is less than the ten-year revenue loss of extending expiring provisions of TCJA and the new policy proposals Donald Trump outlined on the campaign trail?

How to fit 7 trillion pounds of sugar into a 2 trillion pound sack

When your desire to cut taxes is big but your concern about the deficit is bigger

There are seven main ways to limit the net dollar loss of extending and building upon the TCJA

1. You can do fewer things – make choices within the TCJA framework
2. You can do all the same things, but make them less generous – smaller deduction, shorter extension
3. You can do all the same things and keep them just as generous, but do so for fewer years
4. You can do all the same things and keep them just as generous, but add some revenue raising provisions to “expand the sack”
5. You can claim that budgetary savings elsewhere (like revenues generated from tariffs) should could toward reducing the size of your plan
6. You can expand the sack by adding spending cuts
7. You can make the pile of the sugar appear smaller by redefining how you measure it (such as by adopting a “current policy” baseline)