House Vote Tees up $4 Trillion Tax Bill for Senate Action

The U.S. House of Representatives voted 215 to 214 on May 22 to advance a nearly $4 trillion tax bill after reaching a compromise on key tax issues, but significant challenges await in the Senate.

House passage marks a major step forward in the reconciliation process for Republicans, who worked for weeks to satisfy competing constituencies and overcome a narrow House majority. The House Rules Committee convened at 1:00 AM on May 21 and met for more than 18 hours before sending the bill to the floor for several hours of deliberations before a 7:00 AM vote on May 22. Republicans lost only five votes, with two voting against the bill along with every Democrat, one voting "present," and two not voting.

Republicans made last-minute changes to the tax title to increase the cap on the state and local tax (SALT) deduction and accelerate the phaseout of energy credits. The tax title that passed the Ways and Means Committee on May 14 was also amended to:

- Increase the rates on global intangible low-taxed income (GILTI), foreign-derived intangible income (FDII), and the base erosion and anti-abuse tax (BEAT) by a fraction of a percent
- Provide an exception to a restriction on the meals deduction
- Ease an asset test for real estate investment trusts
- Remove some tax increases for tax-exempt entities
- Create a limit on the value of itemized deductions for the top income brackets
- Reduce the excise tax on remittances
- Remove the repeal of the excise tax on indoor tanning services
- Lower the AMT exemption and phaseout thresholds

The legislation remains far from finished. The bill now goes to the Senate, where substantial changes are likely. The Joint Committee on Taxation (JCT) had not yet released an updated cost estimate of the tax title at the time of writing, but House Republicans were working with a $4 trillion tax cap set by their own reconciliation instructions. According to the earlier JCT estimates, the net cost of addressing the expiring provisions in the Tax Cuts and Jobs Act is approximately $4 trillion itself, with Republicans including nearly $7 trillion in extensions and enhancements of TCJA tax cuts and nearly $3 trillion in TCJA tax increase extensions. The bill also includes nearly $1 trillion in new tax cuts balanced against $1 trillion in new revenue raising provisions.

Takeaway

Republicans may have more room for tax cuts as the bill moves to the Senate. The Senate reconciliation instructions provide for the use of a current policy baseline that would assume no revenue impact from extending TCJA provisions. This baseline would erase the nearly $4 trillion net cost of TCJA extensions and allow up to $1.5 trillion in new net tax cuts. Questions remain, however, over whether this could trigger procedural challenges or run into opposition from House deficit hawks.

The Senate will now take up the legislation a mere five weeks before Republicans' July 4 target date for enactment. That deadline may be ambitious and key senators have indicated that enactment before the August recess may be a more realistic goal. The debt limit could give that deadline more urgency. Treasury Secretary Scott Bessent recently told lawmakers that the federal government could default in August unless the reconciliation bill (or other legislation) raises the debt limit. The technical deadline for the reconciliation bill under the budget resolution is Sept. 30, when the government's current fiscal year ends.

Senate Republicans are considering bypassing committee markups in favor of negotiating a Senate package at the leadership level and taking it straight to the floor. Bypassing committees could speed up the process, but could also create complex negotiations and raise procedural issues.

Either way, tax changes are likely. House and Senate Republicans are largely aligned on the key overall tenets of a tax package, but there are differences in the priorities for members of each chamber. Senate Republicans could seek a variety of changes, including softening the cuts to energy credits, making the changes to bonus depreciation and other business provisions permanent, and adjusting the new reciprocal tax on "unfair foreign taxes."

Senate rules will also play an important role. There is little precedent for using a current policy baseline to score reconciliation tax legislation. Republicans have asserted that the Senate parliamentarian reviewed the budget resolution and "deemed it appropriate," but it is not clear how thoroughly all potential issues were vetted.

In addition, there is a separate reconciliation rule that requires every provision in a reconciliation bill to have a revenue impact that is more than "merely incidental." This could result in culling some House provisions with minimal revenue impact. More importantly, it could require changes to the extension of TCJA tax provisions if the current policy baseline scores the extension as having no revenue impact. The House bill may have partially addressed some of these issues by changing the inflation adjustments for the tax brackets and amending the transfer tax exemptions and Section 199A deduction.

Takeaway

The biggest hurdle for Republicans is still the cost. The Senate reconciliation instructions require little in the way of spending cuts and allow for deeper tax cuts. Many moderate Senate Republicans are uncomfortable with the House spending cuts. House and Senate deficit hawks, meanwhile, are deeply committed to the aggressive spending cuts and wary of large tax cuts without offsets. Republicans will have to thread a needle between these two factions to achieve a bill.

The House bill includes meaningful tax changes for nearly all individuals, businesses, and investors, with implications that would be felt across most industries. Key tax cut provisions for businesses include:

- Reinstating 100% bonus depreciation for property placed in service after Jan. 19, 2025, and before Jan. 1, 2029
- Expanding bonus depreciation to cover buildings that manufacture, produce, or refine tangible personal property
- Restoring the expensing of domestic research expenses under Section 174 for tax years beginning in 2025 through 2029
- Amending the limit on the interest deduction under Section 163(j) to add back depreciation and amortization expenses in determining adjusted taxable income for tax years beginning in 2025 through 2029
- Making permanent the current GILTI, FDII, and BEAT effective rates with very minor increases

The bill would generally make permanent all the individual TCJA provisions expiring in 2026 with some adjustments, including:

- Increasing the Section 199A deduction from 20% to 23%
- Increasing the lifetime exemption for the estate, gift, and generation-skipping transfer taxes to $15 million in 2026 (indexed to inflation thereafter)
- Increasing the cap on the SALT deduction to $40,000 for taxpayers with income under $500,000, with those thresholds increasing by 1% for eight years
- Limiting taxpayers' ability to use state pass-through entity (PTE) workarounds for the individual SALT cap
- Changing the treatment of suspended losses under the active loss limit in Section 461(l).
- Restricting the value of itemized deductions for taxpayers in the top bracket

Takeaway

The SALT cap provision was increased from a $30,000 cap and $400,000 income threshold in the original tax title that passed the House Ways and Means Committee on May 14. The compromise provision provided enough relief to gain the support of "SALT caucus" members who were threatening to block the bill, but it will also be tested on the Senate side.

The bill includes four new income tax deductions costing $293 billion intended to fulfill four promises President Donald Trump made to remove tax on tips, overtime, Social Security payments, and auto loan interest on domestic vehicles. The deductions would be in place from 2025 to 2028 and would be available regardless of whether taxpayers itemize their deductions. There are important limitations and income phaseouts for each provision, and employers and other entities would be required to perform new reporting.

The bill would raise $1 trillion with a series of new revenue raising tax increases (not including extensions of the SALT cap or the repeal of personal exemptions).

Many of these provisions could still face resistance from business lobbyists and sympathetic Republican senators. Key provisions include:

- Repealing, phasing out, and restricting many of the energy credits created or enhanced by the Inflation Reduction Act (IRA)
- Increasing the university endowment tax from a 1.4% rate to a top rate of 21%
- Increasing the tax rate on private foundations to a top rate of 10%
- Creating a “floor” for corporate charitable deductions of 1% of taxable income
- Imposing new reciprocal taxes for “unfair” foreign taxes
- Adding new aggregations rules to the limit on deducting executive compensation under Section 162(m)

The tax title omits several key proposals that were under discussion. Some of these provisions could still be considered later in the process, including:

- Providing a 15% corporate rate for domestic manufacturing
- Limiting the corporate SALT deduction
- Increasing the top individual rate
- Changing the taxation of carried interest
- Increasing the 1% stock buyback excise tax

Takeaway

Although the bill is far from final, House passage gives taxpayers a view of core aspects of the package and the operation of important provisions. Taxpayers should begin assessing the impact and considering planning options both before and after enactment. The following is a more detailed discussion of the provisions and their outlook for enactment.

Bonus Depreciation

The bill would restore 100% bonus depreciation for property placed in service after Jan. 19, 2025, and before Jan. 1, 2030. There would be no phasedown beyond these dates, so property placed in service in 2030 or later would not qualify for any bonus depreciation amount.

The legislation would also create a new elective 100% depreciation allowance under Section 168(n) for any portion of nonresidential real property that is considered “qualified production property.” Qualified production property must be original use depreciable property used by a taxpayer in the U.S. as an integral part of a qualified production activity. A qualified production activity includes the manufacturing of tangible personal property, agricultural production, chemical production, or refining. Qualified production property does not include any portion of building property that is used for offices, administrative services, lodging, parking, sales activities, research activities, software engineering activities, or other functions unrelated to qualified production activities.

There is an exception from the original use requirement if acquired property was not used in a qualified production activity between Jan. 1, 2021, and May 12, 2025.

Special recapture rules would apply if the property is disposed of within 10 years after it is placed in service. This provision would apply if construction began on the property after Jan. 19, 2025, and before January 1, 2029. The property is required to be placed in service by the end of 2032.

The bill would also increase the Section 179 deduction to $2.5 million with a phaseout threshold of $4 million, indexed to inflation.

Takeaway

The ability for producers, refiners, and manufacturers to fully expense buildings rather than depreciate them over 39 or 15 years offers a significant benefit. Republicans have indicated that this provision is meant to help fulfill the policy objective underlying Trump's push for a 15% rate on domestic manufacturing. The provision could pose compliance challenges regarding the determination of whether an activity qualifies under the definition of production. Taxpayers with buildings that house both qualified production activities and other administrative, office, or research functions would also likely need to perform an analysis to allocate costs between functions.

Section 174 Research Expensing

The bill would restore expensing of domestic research costs for tax years beginning after Dec. 31, 2024, and before Jan. 1, 2030. The legislation would not reinstate the expensing rules under Section 174, but would instead create temporary rules under new code Section 174A similar to the Section 174 rules before the TCJA changes. Taxpayers would retain the option of electing to capitalize domestic Section 174 costs and amortize such amounts over 10 years or the useful life of the research (with a 60-month minimum). Foreign research would still need to be amortized over 15 years.

Transition rules would require taxpayers to implement the new treatment with an automatic accounting method change on a cut-off basis. The legislation would also address an issue with Section 280C by definitively requiring taxpayers to reduce their deduction for research costs under Section 174A by the amount of any research credit.

Takeaway

Before the TCJA, Section 280C generally required taxpayers to reduce their deduction for research costs by the amount of any research credit or reduce their credit by an equivalent amount. Under changes made by the TCJA, many taxpayers took the position that they were required to reduce their Section 174 capital account only to the extent the research credit exceeded their current year amortization deduction. For most taxpayers, this meant the amortization deduction was allowed in full. The legislation would reverse this "double-dipping" treatment for tax years beginning after 2024 when Section 174A is in effect. It appears that taxpayers could revert to the more favorable treatment when five-year amortization rules become effective again in 2030 after the expiration of Section 174A.

Section 163(j) Limit on the Interest Deduction

The bill would reinstate the more favorable calculation of the limit on the interest deduction under Section 163(j) for tax years beginning after Dec. 31, 2024, and before Jan. 1, 2030. Section 163(j) generally limits the interest deduction to 30% of adjusted taxable income (ATI). For tax years beginning after 2021, current law requires ATI to include amortization, depreciation, and depletion. The bill would once again remove amortization, depreciation, and depletion from the ATI calculation.

Takeaway

The temporary nature of this provision and the changes to bonus depreciation and research expensing would create lingering uncertainty for multiyear tax planning. There is interaction between the provisions, so taxpayers should model out various scenarios, particularly because some outcomes could result in a permanent impact. For taxpayers that may still face interest expense limitations even after enactment, there may be options to apply planning strategies such as interest capitalization to utilize tax attributes aggressively.

Section 199A

The bill would make the deduction for pass-through income under Section 199A permanent with several enhancements. The deduction rate would increase from 20% to 23% for taxable years beginning after Dec. 31, 2025. The bill would also adjust the phaseout of the deduction for taxpayers who do not meet the wage expense and capital investment requirements or who participate in a disqualified “specified trade or business.” The deduction would be reduced by 75% of the amount that the taxpayer’s income exceeds the phaseout threshold (if greater than the deduction allowed by applying the regular limits). The bill would also allow dividends from business development companies to qualify for the deduction.

Takeaway

The change in the phaseout rules offers a better result for taxpayers whose income exceeds the taxable income thresholds ($197,300 for single filers and $394,600 for joint filers in 2025) and who would not otherwise qualify for Section 199A under the regular rules. The increase in the deduction from 20% to 23% would bring the top effective rate on qualifying income down from 29.6% to 28.5%. The effective rate cut is somewhat modest, but there may be rate arbitrage opportunities to accelerate deductions to 2025 and defer qualifying income to 2026. If the top individual marginal rate were allowed to revert from 37% to 39.6%, then increasing the deduction to 23% would reduce the top effective rate from 31.7% to 30.5%.

SALT Cap

The bill would effectively create a permanent SALT cap, but with several important changes. The legislation removes the temporary $10,000 limit on SALT deductions under Section 164, and instead creates a new permanent limit of $40,000 for both single and joint filers under Section 275 beginning in 2025. The increased cap would begin to phase down to $10,000 when modified gross income exceeds $500,000. The $40,000 cap and $500,000 phaseout would increase by 1% each year from 2026 through 2033 and then remain static.

> **Takeaway**
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> The final agreement represents an increase over the $30,000 cap and $400,000 income phaseout in the version passed by the House Ways and Committee. The compromise was the product of intense negotiations, and ultimately proved generous enough to win support from several Republican holdouts who were threatening to block the bill over the issue.

The Section 275 limit would apply to specified state income, sales, and property taxes (as well as foreign income taxes and taxes paid by cooperative housing corporations), and includes a provision designed to shut down state law pass-through regimes that allow “workarounds” to the SALT cap. The state laws generally allow pass-through entities to pay tax at the entity level where it can be deducted in full, and then provide a credit or exclusion to the business owners so the income is not taxed again by the state at the individual level.

The bill would deny partnerships and S corporations the ability to deduct specified taxes under Section 275, and instead would require the taxes to be passed through to owners as separately stated items. The separately stated taxes would be subject to the $40,000 cap at the individual level as “substitute payments” if made in exchange for tax benefits provided to individual owners. There would be an exception for property taxes paid at the entity level and income taxes paid by a partnership or S corporation if at least 75% of the gross receipts are derived in a qualified trade or business under Section 199A. The final legislative language also seeks to clarify that sales taxes incurred by a business would not be covered by the new restrictions.

> **Takeaway**
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> The rules are complex, but the provision appears to largely shut down state law SALT cap workarounds, with an important exception for businesses qualifying under Section 199A. For businesses that would not qualify for the exception, the inability to deduct state taxes at the federal level in the pass-through form could prompt an assessment of entity choice, particularly in high-tax states or in anticipation of significant income events.

FDII, GILTI, and BEAT

The bill would prevent a large scheduled decrease in the Section 250 deduction, instead creating a permanent effective rate near the current rate with a slight decrease in the deduction. Under the bill, the current effective rate on FDII would increase from 13.125% to 13.335% (it was set to rise to 16.4%) and the current effective rate on GILTI would increase from 10.5% to 10.668% (it was set to rise to 13.125%). The bill would also exclude from the definition of GILTI tested income any "qualified Virgin Islands services income."

The legislation would similarly create a permanent BEAT rate of 10.1%, up from 10% but preventing a larger increase to 12.5%. The bill also repeals an unfavorable change to the BEAT scheduled to take effect in 2026 that would have effectively required taxpayers to increase their liability by the sum of all income tax credits.

Reciprocal Tax for "Unfair Foreign Taxes"

The legislation would add new Section 899, which would impose retaliatory taxes on residents of "discriminatory foreign countries" that impose "unfair foreign taxes."

The provision is largely based on the Defending American Jobs and Investment Act (H.R. 591) and the Unfair Tax Prevention Act (H.R. 2423), which were introduced earlier this year by Republicans on the House Way and Means Committee. The legislation would essentially raise the tax and withholding rates for affected foreign taxpayers on several types of income, including:

- Fixed, determinable, annual, or periodical (FDAP) income and other income of a nonresident alien under Sections 871(a)(1), 871(a)(2), and 1445(a)
- Effectively connected income (ECI) of a foreign corporation under Section 882(a) and a nonresident alien under Section 871(b)
- FDAP and other income imposed on U.S.-source income of foreign corporations under Section 881(a)
- Branch dividend equivalents under Section 884
- U.S.-source investment income of foreign private foundations under Section 4948
- Dispositions of U.S. real property interests under Section 1445(e)

The legislation would also modify how BEAT applies to corporations that are more than 50% owned by affected foreign taxpayers. These corporations would be subject to BEAT at a 12.5% rate regardless of whether they met the applicability thresholds under the gross receipts and base erosion tests. These corporations would lose the ability to reduce their BEAT liability using tax credits. The legislation would also eliminate the services cost method exception from base erosion payments and treat capitalized payments of corporations that are more than 50% owned by affected foreign taxpayers as base erosion payments.

The definition of unfair foreign taxes is relatively broad and includes the undertaxed profits rule under Pillar Two, digital service taxes, and "any other tax with a public or stated purpose indicating the tax will be economically borne, directly or indirectly, disproportionately by United States persons." The provisions also target "extraterritorial taxes" and "discriminatory taxes," with fairly broad definitions for both.

The additional rates imposed under the legislation would not replace treaty rates, but would impose additional incremental tax on top of treaty rates.

Takeaway

Lawmakers appear to be trying to avoid overriding treaties, but it is unclear whether other countries would consider these taxes a treaty violation or how they would react to the proposal in general. The taxes would be significant and punitive and don't offer many mechanisms for compromise with foreign countries. The provision is essentially self-executing for tax years beginning after the later of 90 days after enactment, 180 days after a foreign country enacts an "unfair" foreign tax, or when the "unfair" foreign tax begins to apply. The provisions could also pose some administrability issues and could be unpopular with some Senate moderates.

Energy Credits

The bill would raise more than $500 billion by repealing, restricting, and phasing out many of the energy credits enacted as part of the Inflation Reduction Act. Several credits would be repealed at the end of 2025, including:

- Previously owned clean vehicle credit under Section 25E for purchases after 2025
- Clean vehicle credit under Section 30D for purchases after 2025 unless the manufacturer has sold fewer than 200,000 clean vehicles since 2010, in which case the credit expires for purchases after 2026
- Commercial clean vehicle credit under Section 45W for purchases after 2025 unless the vehicle was acquired pursuant to a written binding contract in place before May 12, 2025
- Alternative fuel refueling property credit under Section 30C for property placed in service after 2025
- Energy-efficient home improvement credit under Section 25C for property placed in service after 2025
- Residential clean energy credit under Section 25D for property placed in service after 2025
- New energy-efficient home credit under Section 45L for property acquired after 2025 unless construction began before May 12, 2025

Takeaway

Taxpayers and manufacturers would have a short runway to accelerate production, projects, and purchases before the end of 2025 to still qualify for the above credits.

The legislation would generally repeal the production tax credit under Sections 45Y and the investment tax credit under Section 48E for projects beginning construction more than 60 days after the date of enactment or placed in service after 2028. Nuclear facilities would still be eligible for the credits, as long as construction began before 2029. The bill would also deny a credit for leasing arrangements of solar and wind property if the lessee could claim a residential credit under Section 25D.

The hydrogen production credit under Section 45V would be repealed for projects beginning construction after Dec. 31, 2025. The advanced manufacturing credit under Section 45X would be repealed for wind energy components sold after 2027 and for all other components sold after 2031.

The legislation would impose new restrictions denying most credits for taxpayers considered foreign entities or concern for tax years beginning after the date or enactment. Taxpayers that are a “foreign influenced entity” would be ineligible for the credits for tax years beginning two years after the date or enactment. The rules are even more restrictive for the Section 48 investment tax credit and the Section 45Y production tax credit. The credits would not be available for facilities receiving “material assistance” from covered foreign entities if construction began after Dec. 31, 2025.

Takeaway

Last-minute changes to the bill accelerated the application of the “material assistance” restrictions, but they may not have much effect because the phaseout of the entire credits under Sections 45Y and 48E takes place even earlier.

The legislation would also change taxpayers’ ability to transfer credits to unrelated taxpayers for cash under Section 6418. Transferability has provided an important monetization option for many projects, but traditional tax-equity financing structures remain viable.

Takeaway

The credit phaseouts could prompt the acceleration of projects, particularly for clean hydrogen. The IRS has long-standing and well-understood rules on how to establish that construction has begun. The early phaseouts could also kill some projects that are not shovel ready. The version that passed the House Ways and Means Committee had longer phaseout periods for the credits, but deficit hawks successfully pushed to accelerate their elimination. There are Republicans in both chambers who support the energy credits, and who could push back against some of these changes as the legislative process continues.

Section 162(m)

The bill would amend the aggregation rules for applying the $1 million limit on deducting the compensation of covered employees of a public company under Section 162(m). The current rules identify covered employees separately for each public entity, but compensation subject to the limitation is calculated on a controlled group basis. The number of covered employees is set to expand by five for tax years beginning in 2027 or later, and there has been some question over whether these employees can come from the entire controlled group or only the public entity.

The bill would create a new aggregation rule for tax years beginning after 2025 for both identifying who is a covered employee and the amount of compensation subject to the limit. The aggregation rules would be based on a controlled group as defined under the qualified plan rules in Section 414. The proposal would also provide rules for allocating the $1 million deduction between members of a controlled group.

Takeaway

The provision would have unfavorable consequences for many companies, including requiring the full amount of compensation from a related partnership in the calculation (rather than a pro-rata amount based on ownership percentage). It is estimated to raise almost $16 billion. Republicans declined to add even more aggressive proposals that were under discussion, including proposals to accelerate the changes taking place in 2027, apply the limit to private companies, or expand the limit to apply to every employee of a company. It's possible these proposals could resurface later in the process if revenue becomes an issue.

Deduction for Tip Income

The bill would provide taxpayers a deduction equal to the amount of qualified tips reported on Forms W-2, 1099-K, 1099-NEC, or 4317. The deduction would be allowed from 2025 through 2028 without regard to whether a taxpayer itemized deductions. There is no cap on the deduction itself, but it is available only to taxpayers whose income does not exceed the threshold of a highly compensated employee under Section 414 ($160,000 in 2025).

For tips to be deductible, they must be paid voluntarily in an occupation that "traditionally and customarily" received tips before 2025, as provided by the Secretary. The business in which the tips are earned cannot be a specified trade or business under Section 199A, and self-employed taxpayers, independent contractors, and business owners face additional limitations.

Employers would be required to report qualifying tips to employees on Form W-2. The provision applies only to income taxes, and generally does not affect the employer's FICA tip credit except to extend it to certain beauty services businesses.

The bill gives Treasury several specific grants of authority to provide regulations on specific issues. The IRS would need to adjust withholding tables and write regulations defining which occupations "traditionally and customarily" received tips in the past. The IRS would also need to provide rules for determining when a tip is voluntary.

The impact of the provision on employers could be meaningful. Hospitality businesses would face new reporting requirements that depend on how the business and worker occupations are characterized. Employees' ability to deduct tips could also depend on employer policies, such as mandatory tips, service charges, or other amounts that are not solely determined by the customer.

Takeaway

In a surprise move, the Senate on May 20 approved by unanimous consent a stand-alone bill with a similar deduction for tips. For now, the House appears unlikely to act on this separate Senate bill and will seek to address the provision as part of the reconciliation process.

Deduction for Overtime Pay

The bill would provide a deduction equal to qualified overtime compensation. The deduction would be allowed from 2025 through 2028 without regard to whether a taxpayer itemized deductions. There is no cap on the amount of overtime that can be deducted, but it would be available only to taxpayers whose income does not exceed the threshold of a highly compensated employee under Section 414 ($160,000 in 2025).

Qualified overtime compensation is defined as compensation paid to an individual required under section seven of the Fair Labor Standards Act (FLSA). Employers would be required to provide new information reporting to separately report overtime pay.

Takeaway

The determination of whether compensation is qualified overtime pay would not be made using tax rules, but would depend on the employer's characterization of the pay under the FLSA.

Auto Loan Interest Deduction

The bill would create an above-the-line deduction for up to $10,000 of interest on a qualified passenger vehicle loan from 2025 through 2028. The deduction would begin to phase out once modified adjusted gross income exceeds $100,000 for single filers or $200,000 for joint filers.

The vehicle must be manufactured primarily for use on public streets, roads, and highways, and final assembly of the vehicle must occur in the U.S. The deduction does not apply to lease financing and the loan cannot be to finance fleet sales, purchase a commercial vehicle, purchase a salvage title, purchase a vehicle for scrap or parts, or be a personal cash loan secured by a vehicle previously purchased by the taxpayer.

Takeaway

Auto loan financing companies would face additional reporting requirements and would be required to furnish a return with specific information on loans.

Deduction for Seniors

The bill would provide a $4,000 deduction for all individuals aged 65 and above. The deduction would be allowed from 2025 through 2028 without regard to whether a taxpayer itemized deductions. The deduction would phase out for taxpayers with modified adjusted gross income exceeding $150,000 for joint filers and $75,000 for all other taxpayers.

Takeaway

The deduction is meant to fulfill Trump's pledge to remove tax on Social Security payments, but because the reconciliation rules preclude changes to Social Security, the bill instead provides a general income tax deduction.

Transfer Taxes

The bill would permanently set the lifetime exemptions for the gift, estate, and generation-skipping transfer taxes at $15 million for 2026, indexing them for inflation thereafter. The change represents a modest increase from the exemptions under the TCJA, which were initially set at $10 million, but reached $13.99 million in 2025 with inflation adjustments.

Active Business Losses

The legislation would make the active loss limit under Section 461(l) permanent, with an important and unfavorable change. The provision was created by the TCJA and was originally set to expire after 2025. It was suspended by the Coronavirus Aid, Relief, and Economic Security (CARES) Act for three years, but then extended through 2026 by the American Rescue Plan Act of 2021 and extended again through 2028 by the Inflation Reduction Act.

The legislation would not only make Section 461(l) permanent, but would require taxpayers to separately track and carry forward disallowed losses to be applied in calculating the Section 461(l) limit in subsequent years. Under current law, a disallowed loss under Section 461(l) generally becomes a net operating loss (NOL) in subsequent years. This allows taxpayers to use an NOL created by Section 461(l) against other sources of income in future years, causing Section 461(l) to act more like a one-year loss deferral mechanism for many taxpayers.

Takeaway

Democrats proposed a similar change as part of IRA negotiations before abandoning it. The provision would add another layer of complexity for individuals, who would be forced to separately apply and track passive losses, at-risk losses, NOLs, and now Section 461(l) losses. It could also make it much harder for taxpayers to deduct disallowed losses in future years.

Individual TCJA Extensions

The bill would make many of the TCJA provisions permanent without change, including:

- Repeal of personal exemptions
- Limits on the deductions for mortgage interest, personal casualty losses, wagering losses, and moving expenses
- Repeal of miscellaneous itemized deduction
- Exclusion for bicycle commuting reimbursements

Many other TCJA individual provisions are amended in significant ways. The increased AMT exemption and phaseout thresholds would be made permanent, but with a change to the inflation adjustment that claws back recent inflation increases beginning in 2026.

The legislation also permanently repeals the Pease limitation on itemized deductions that was suspended by the TCJA through 2025, but creates a new limit. The new provision would essentially cap the value of itemized deductions. The maximum benefit achievable for the deductions would be equivalent to offsetting income taxed at a top rate of 32% rather than offsetting income taxed at the higher individual marginal rates of 35% and 37%.

The legislation would also make permanent the increased standard deduction and child tax credit with enhancements. The standard deduction would be further increased by $1,000 for single filers and $2,000 for joint filers from 2025 to 2028. The child tax credit would increase by $500 from 2025 to 2028. It would be indexed to inflation after reverting to $2,000 in 2029. Social Security numbers would also be required.

The bill would make permanent the individual rate cuts and bracket adjustments, while adding a slightly more favorable inflation adjustment for every bracket except the 37% bracket.

Takeaway

The legislation does not increase the top individual rate despite Trump reportedly pushing Republicans to revert the top rate to 39.6%. Trump's public comments have been mixed. He initially said he opposed increasing the top rate because it would cause the wealthy to flee the country. In a subsequent interview, he said he liked the idea of raising taxes on the "wealthy" to "take care of the middle class," adding, "I actually love the concept but I don't want it to be used against me politically because I've seen people lose elections for less."

> In a later social media post, he said he would “graciously accept” a tax increase on the “rich,” adding that “Republicans should probably not do it, but I’m okay if they do.” Influential conservative and House Freedom Caucus Chair Andy Harris, R-Md., has expressed interest in the idea, but the proposal has generally been unpopular with congressional Republicans, including House Speaker Mike Johnson, R-La.

Opportunity Zones

The bill would extend the deadline for making an opportunity zone investment from Dec. 31, 2026, to Dec. 31, 2028. The legislation would also modify the rules for designating opportunity zones, creating a new category of rural opportunity zones with more favorable rules. The mandatory recognition date for deferred gain for investments made in 2027 or 2028 would be Dec. 31, 2033, and taxpayers would receive a 10% increase in basis for holding onto the property for five years. Taxpayers could also designate up to $10,000 of their aggregate investments to offset ordinary income, with no recapture. The provision would impose new reporting requirements on taxpayers making investments.

Form 1099 Reporting

The bill would amend Section 6050W to reinstate the 200 transaction and $10,000 threshold for reporting third-party payment network transactions on Form 1099-K. The American Rescue Plan Act (ARPA) of 2021 repealed that threshold and required reporting when aggregate payments exceeded $600 without regard to the number of transactions. The IRS offered transition relief delaying the implementation of the change for two years, and then provided a $5,000 threshold for payments made in 2024 and a $2,500 threshold for payments made in 2025. The bill would restore the old threshold retroactively so that reporting would be required only if aggregate transactions exceeded 200 and aggregate payments exceeded $10,000.

The bill would also increase the threshold for reporting payments under Sections 6041 and 6041A on Forms 1099-MISC and 1099-NEC from $600 to $2,000 in 2026, indexing that figure to inflation in future years.

Tax-Exempt Entities

The legislation includes numerous provisions aimed at tax-exempt entities, and universities in particular. Key provisions would:

- Replace the 1.4% endowment tax rate with graduated brackets based on the size of the endowment per student, reaching a top rate of 21% (while providing a new exception to the tax for certain religious universities)
- Replace the 1.39% excise tax on private foundations with graduated brackets based on assets, reaching a top rate of 10%
- Revise the excise tax on executive compensation to include all current and former employees

- Expand the rules for determining unrelated business taxable income (UBTI) to include qualified transportation fringe benefits such as parking and transit passes and to narrow the exception for research income so it applies only to research freely available to the general public.

Takeaway

The original version of the bill passed by the House Ways and Means Committee included provisions adding name and logo royalties to UBTI and giving the Treasury Secretary authority to revoke an organization's tax-exempt status based on "support" for "terrorist organizations." The legislation also would have expanded the excise tax on executive compensation to related parties. All these changes were removed from the bill before it passed the House.

Employee Retention Credit

The legislation would make several changes to the employee retention credit (ERC), including:

- Barring ERC refunds after the date of enactment for claims filed after Jan. 31, 2024
- Extending the statute of limitation on ERC claims to six years
- Increasing preparer and promoter penalties on ERC claims

Takeaway

The provision would presumably affect only refund claims that have not been paid by the IRS. The legislative language provides that no credit or refund "shall be allowed or made after the date of enactment," unless the claim was filed on or before Jan. 31, 2024. The IRS had been slow to process claims filed after Jan. 31, 2024, potentially in anticipation this provision, which had been included in a failed tax extenders bill from 2024. The provision is now estimated to raise only $6.3 billion, much less than the $77 billion estimated for the 2024 version. The difference may be due to refunds that have already been paid, although it remains unclear how fast the IRS is currently processing claims filed after Jan. 31, 2024.

Other Provisions

The bill includes many other potentially important provisions for taxpayers, including

- Increasing the threshold for certain taxpayers to use the cash method of accounting and other favorable accounting rules from $25 million in gross receipts to $80 million
- Imposing a 3.5% excise tax on remittances that could have broad implications for payment processors and financial accounts
- Creating a 1% floor for charitable deductions for corporations by providing that a deduction is allowed only to the extent it exceeds 1% of taxable income (up to the current 10% cap) for tax years beginning after 2025
- Increasing and modifying the low-income housing tax credit for 2026 through 2029

- Allowing taxpayers purchasing professional sports franchises to amortize only 50% of intangibles under Section 197
- Creating new tax-preferred accounts for children, with a pilot program offering a $1,000 contributory credit for qualifying children
- Allowing individual taxpayers who don't itemize a charitable deduction of up to $300 for joint filers and $150 for other taxpayers for tax years 2025 through 2028
- Raising the percentage of allowable assets a REIT may have in a qualified REIT subsidiary from 20% to 25% effective for tax years beginning after 2025
- Providing an exception to the restriction on deducting meals provided at the convenience of an employer that is scheduled to take effect in 2026, so that it would not apply to meals sold by the taxpayer in a bona fide transaction for adequate and full consideration
- Changing the explicit regulatory mandate for the rules under Section 707(a)(2)
- Amending numerous health care tax rules

Next Steps

The tax title is not final, but the House bill offers important insight into Republican priorities and the technical operation of various proposals. Taxpayers should assess the potential impact of major provisions when considering the tax efficiency of transactions and investments. There may be planning opportunities that should be considered now, such as accelerating or abandoning energy credit projects or investments and modeling the impact of changes to the limit on the interest deduction under Section 163(j), bonus depreciation, and research expensing under Section 174.