House taxwriters approve US-Taiwan tax pact

After several months of jurisdictional negotiations, a compromise reached between two Senate panels this week enabled the House Ways and Means Committee to pass legislation allowing for an agreement with Taiwan that would reduce double taxation on Taiwanese companies operating in the US. The breakthrough on the tax agreement, which is of particular importance to the semiconductor industry the US is looking to strengthen, could mean that a bill makes its way to the president before year-end.

While such an agreement with a trading partner would typically be a bilateral tax treaty, the US cannot sign such a treaty with Taiwan because of the “One China” policy, under which the US recognizes the People’s Republic of China (PRC) as the sole legal government of China, therefore maintaining formal relations with the PRC and only unofficial relations with Taiwan. As a result, the legislation moving through Congress would authorize negotiations on a tax agreement to be conducted through the American Institute in Taiwan (AIT) and the Taipei Economic and Cultural Representative Office (TECRO), rather than directly between the US and Taiwan.

How we got here

The Senate Foreign Relations Committee, which under normal circumstances has jurisdiction over tax treaties, passed the Taiwan Tax Agreement Act of 2023 (S. 1457) on July 25, authorizing the administration to negotiate an agreement on cross-border tax issues between the US and Taiwan. This approach would obviate the need for changes to the US tax code, but Finance Committee leaders argued that their subject-matter expertise is important for this unique situation and that changes to the US tax code can be done more quickly. The Senate Finance Committee unanimously approved the US-Taiwan Expedited Double Tax Relief Act (S. 3084) on September 14, and the two committees agreed to work towards a compromise approach.
URL: https://www.congress.gov/bill/118th-congress/senate-bill/1457/text
URL: https://www.congress.gov/118/bills/s3084/BILLS-118s3084rs.pdf

In a statement November 29, Finance Committee Chairman Ron Wyden, D-Ore., and ranking member Mike Crapo, R-Idaho, along with Foreign Relations Chairman Ben Cardin, D-Md., and ranking member Jim Risch, R-Idaho, announced they had reached that compromise: a bill with two titles incorporating much of both committees’ language, which was easily approved by voice vote at a Ways and Means Committee mark-up on November 30.

Title I of the negotiated bill (H.R. 5988, offered as an amendment in the nature of a substitute by Ways and Means Committee Chairman Jason Smith, R-Mo.) comprises the Senate Finance-passed US-Taiwan Expedited Double Tax Relief Act, which would provide benefits for income from US sources earned or received by qualified residents of Taiwan, including reduced tax rates, taxation of only that income effectively connected with a US permanent establishment, and preferential treatment of wages and related income earned by qualified residents. According to a description provided by the Joint Committee on Taxation (JCT) staff, these rules are “analogous to provisions typical in bilateral treaties to which the [US] is a party.” The proposed rules

would apply only if the US Treasury secretary certifies that reciprocal provisions are put in place for US persons with respect to income sourced in Taiwan.
URL: https://gop-waysandmeans.house.gov/wp-content/uploads/2023/11/AINS-to-H.R.-5988.pdf
URL: https://www.jct.gov/publications/2023/jcx-52-23/

Title II comprises the United States-Taiwan Tax Agreement Authorization Act, which authorizes the president to negotiate additional tax benefits between the US and Taiwan beyond those provided for in Title I but limits any such negotiations to benefits addressed in the US's model tax treaty. This section requires the president to notify Congress before negotiations begin and to provide periodic updates on talks and requires Congress to pass both approval legislation and implementing legislation before any benefits could take effect.

"Taiwan—one of the world's largest economies—is among the United States' top trading partners, yet the only such partner without an agreement to address double taxation," the senators said in their statement. "Our bills not only rectify this problem, but facilitate broader investment between the United States and Taiwan, create more American jobs across the country, and help promote our collective prosperity, national security, and economic resilience."

Next steps: Congressional passage by year-end?

Many businesses, and especially those in the semiconductor industry, hope the legislation will become law before the end of this year. Following on 2022's CHIPS and Science Act (P.L. 117-167), lawmakers anticipate attracting more advanced semiconductor manufacturing—especially from Taiwan, where 60 percent of all chips are currently produced—but industry officials and legislators argue that the costs are prohibitive in part due to the lack of an agreement to prevent double taxation. Without a tax agreement, Taiwan's corporations face a 30 percent withholding tax on dividends, interest, and royalties in the US, compared with rates as low as 5 percent (and, in certain instances, even zero) for some companies from countries that have tax treaties with the US.
URL: https://www.congress.gov/117/plaws/publ167/PLAW-117publ167.pdf

Ways and Means Chairman Jason Smith told reporters this week that he has discussed the bill with House leadership and is optimistic it will be voted out of the chamber quickly. The question for those in the tax policy arena is the process by which that might happen. This late in the calendar year, as the number of legislative days dwindles, smaller bills are often attached to much larger "must pass" measures, such as omnibus appropriations legislation to fund federal government operations. However, with the annual federal spending process now kicked into early 2024, such vehicles are in shorter supply than usual this year. (Congress recently passed a "laddered" continuing resolution extending funding into late January of next year for some federal department and agencies and early February for others. For additional details, see *Tax News & Views*, Vol. 24, No. 39, Nov. 17, 2023.)
URL: https://dhub.deloitte.com/Newsletters/Tax/2023/TNV/231117_1.html

"We'll take whatever vehicle we can," Senate Foreign Relations Committee Chairman Cardin told reporters ahead of the Ways and Means vote.

Also in search of an engine to pull it across the finish line is a trio of tax provisions many businesses have spent two years pushing for: retroactive repeal of mandatory amortization of research and development expenses and of stricter limits on the expensing of business interest deductions, which both took effect in 2022, and a retroactive return to full expensing of capital investment, which began phasing out this year. Democrats insist the three provisions must be paired with tax relief for families, such as an expanded child tax credit.

While there has been much behind-the-scenes negotiating among taxwriting staff and members to craft such a package—estimated to cost about $100 billion in revenue, split fairly evenly between the business and individual provisions—key players say there is still no deal and no obvious vehicle in sight. (See separate coverage in this issue for a discussion about how the IRS's recent announcement of additional administrative relief from more stringent 1099-K reporting requirements that had been scheduled to take effect in 2024 has complicated congressional efforts to reach a deal on a tax package in the near term.)

Two other tax measures also reported favorably

In addition to the tax agreement with Taiwan, the Ways and Means Committee also approved two other pieces of tax legislation at the November 30 mark-up—both of them relatively narrow and noncontroversial.

The first measure—reported to the full House by a unanimous 41-0 vote—was H.R. 6408, legislation that was introduced on November 14 by taxwriters David Kustoff, R-Tenn., and Rep. Bradley Schneider, D-Ill.
URL: https://www.congress.gov/bill/118th-congress/house-bill/6408/text

In general, the legislation would seek to terminate the tax-exempt status of terrorist-supporting organizations. Under current law, tax code section 501(p) serves to suspend the tax exemptions of certain US-based "terrorist organizations" named by the IRS. H.R. 6408 would similarly suspend the tax exemption of named terrorist-supporting organizations (that is, an entity that provides material support or resources to a terrorist organization). The JCT staff has estimated that the measure would have a negligible impact on federal revenues.
URL: https://www.jct.gov/publications/2023/jcx-53-23/

The second tax measure—reported by a unanimous 42-0 vote—was H.R. 1432, the VSO Equal Tax Treatment Act, or "VETT" Act. That bill, which was introduced on March 3 by House taxwriters Brad Wenstrup, R-Ohio, and Jimmy Panetta, D-Calif., would expand the deductibility of charitable contributions to all federally chartered tax-exempt organizations serving current and former members of the armed forces (that is, organizations described in tax code section 501(c)(19)) by superseding a rule that currently requires such organizations to maintain a membership of at least 90 percent wartime veterans in order to receive tax-deductible contributions.
URL: https://www.congress.gov/bill/118th-congress/house-bill/1432/text

According to the JCT staff, H.R. 1432 is estimated to reduce federal revenues by roughly $1 million over the next decade.
URL: https://www.jct.gov/publications/2023/jcx-54-23/

The panel also approved three nontax bills at the mark-up that would modify the Social Security Act and US Customs rules.

Subcommittee hearings ahead

In other Ways and Means developments this week, two subcommittees announced plans to hold separate hearings on December 6.

- **Federal debt:** The Oversight Subcommittee will hold a hearing at 10:00 a.m. on December 6 to examine the drivers of the rapidly rising cost to service federal debt and US debt management practices.
- **Expanding economic growth:** The Tax Subcommittee will hold a hearing at 2:00 p.m. on December 6 to discuss the benefits of pro-growth tax policy for American families, workers, and small businesses.

Witness lists for the two hearings were not available at press time.

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