Senate Finance Republicans generally align with House-passed plan, but key differences remain

Senate Finance Committee Chairman Mike Crapo (R-Idaho) released the tax portion of the Senate's version of the One Big Beautiful Bill Act (OBBBA), a proposal aimed at permanently extending the individual, passthrough, and business tax provisions of the Tax Cuts and Jobs Act of 2017 (TCJA, P.L. 115-97) and creating new tax benefits aligned with campaign promises designed to provide additional relief for individuals and families. The proposal also includes revisions to raise revenue as well by, among other means, modifying international tax rules and the clean energy tax credits enacted in the Inflation Reduction Act (P.L. 117-169) – the latter of which has been a source of debate both within and between House and Senate Republicans, highlighting differing priorities within the GOP. This package is a response to the tax portions of the OBBBA that was approved late last month by the House of Representatives. (For prior coverage of the House-passed bill, see *Tax News & Views*, Vol. 26, No. 19, May 14, 2025; *Tax News & Views*, Vol. 26, No. 22, May 23, 2025.)
URL: https://www.congress.gov/115/plaws/publ97/PLAW-115publ97.htm
URL: https://www.congress.gov/117/plaws/publ169/PLAW-117publ169.pdf
URL: https://dhub.deloitte.com/Newsletters/Tax/2025/TNV/250514_1.html
URL: https://dhub.deloitte.com/Newsletters/Tax/2025/TNV/250523_1.html

The Finance Committee's proposal reflects the Senate's distinct political and policy priorities, setting it apart from the House approach. Notably, while both the Finance and the House Ways and Means Committees revised the cap on the state and local tax (SALT) deduction, their approaches differ significantly. The House bill – shaped by negotiations with moderate Republicans from high-tax states – would raise the cap to $40,000 (subject to an income phase-out) starting in 2025, while in contrast, the Finance Committee's proposal, led by Chairman Crapo, would extend the cap at its current level of $10,000 after its scheduled expiration at the end of this year. Notwithstanding this provision, the explanatory materials note that the Senate expects this to be a subject of continuing negotiations as the legislative process advances. The divergent provisions underscore the limited appetite among Senate Republicans – none of whom represent the highest-tax states – for a more generous SALT deduction, despite House members' insistence that the $40,000 cap was essential to securing their support.

The Finance Committee also made several changes to section 899 – a new provision in the House-passed bill that would impose retaliatory tax measures on jurisdictions enacting so-called "unfair foreign taxes," such as the undertaxed profits rule, digital services taxes, and other taxes on American taxpayers deemed discriminatory or extra-territorial. In addition to a delayed effective date for this provision, the Senate's other changes would also have a lower cap on how much tax rates on covered companies and individuals could rise.

The Finance Committee proposal also diverges from the House-passed bill in its treatment of key business provisions: it would permanently extend 100 percent bonus depreciation, the immediate deduction for domestic research and experimental expenses, and a more generous calculation of the amount of net business interest expense that can be deducted – whereas the House-passed bill extended these provisions only temporarily, through 2029.

At the procedural level, with a budget resolution in place, the Republicans are advancing their tax and spending legislation through reconciliation – a process that allows passage with simple majorities in both chambers, bypassing the usual 60-vote threshold in the Senate. This procedural advantage has significantly influenced the design and scope of the Senate's tax package.

A key factor shaping the final size and duration of any tax changes is the difference in budget assumptions used by the House and the Senate. Unlike the House, which uses a "current law" baseline and accounts for the revenue impacts of extending expiring provisions of the 2017 tax law, the Senate relies on a "current policy" baseline that assumes those provisions were always meant to be permanent and therefore there is no revenue lost from extending them. This difference in baseline assumptions is central to how the revenue impacts of proposed tax changes are calculated and ultimately influences what can be included in the final legislation that reaches President Trump's desk.

The Finance Committee's website features legislative text, a section-by-section summary of the proposal, and an overview. As of press time, the Joint Committee on Taxation has not provided a revenue estimate of the package.
URL: https://www.finance.senate.gov/imo/media/doc/finance_committee_legislative_text_title_vii.pdf
URL: https://www.finance.senate.gov/imo/media/doc/finance_committee_section-by-section_title_vii3.pdf
URL: https://www.finance.senate.gov/imo/media/doc/finance_committee_summary1.pdf

What's here, what's ahead…

This special edition of *Tax News & Views* offers an overview of the tax package, makes observations on key provisions, and looks at the key areas in which the Finance Committee proposal differs from the Ways and Means proposal.

Business-related deductions, credits, and other items of note

The Finance Committee's newly released tax package includes a broad set of provisions impacting corporations and other business entities. Collectively, these measures reflect the GOP's continued hope that this package would contribute to economic expansion, innovation, and long-term fiscal strength.

Full expensing of domestic research and experimental expenditures: The Finance Committee's tax proposal would add new section 174A to permanently allow an immediate deduction of domestic research or experimental expenditures paid or incurred by the taxpayer during taxable years beginning after December 31, 2024. New section 174A would permit a taxpayer to elect to capitalize and amortize domestic research or experimental expenditures ratably over a period of no less than 60 months, beginning with the month in which the taxpayer first realizes benefits from the expenditures. The election must be made by no later than the due date of the taxpayer's federal income tax return (including extensions) and would apply to the tax year for which the election is made and all subsequent tax years unless the taxpayer receives consent to change to a different method or period. A conforming modification to section 59(e)(2)(B) allows a taxpayer to elect to capitalize and recover domestic research or experimental expenditures over ten years beginning in the taxable year such expenditures are paid or incurred.

With respect to section 174(d) that continues to apply to specified research and experimental (SRE) expenditures for foreign research, the House bill would amend the rule such that there is no deduction or reduction to amount realized with respect to the unamortized balance of the SRE expenditures on account of the disposition, retirement, or abandonment of property with respect to which SRE expenditures are paid or incurred. The amendments would apply to property disposed, retired or abandoned after May 12, 2025.

The tax proposal would provide coordination between new section 174A and sections 41(d)(1)(A) and 280C(c), that requires that a taxpayer reduce the new section 174A deduction by the credit claimed, or alternatively, elect to claim a reduced section 41 research credit.

The amendments under the proposal would generally apply to amounts paid or incurred in taxable years beginning after December 31, 2024. The amendments are treated as a change in method of accounting made on a cut-off basis for any research or experimental expenditures paid or incurred in taxable years beginning after December 31, 2024.

The Senate language would add special transition rules that would allow for small business taxpayers that meet the gross receipts test under section 448(c) for the first taxable year beginning after December 31, 2024, to retroactively elect to apply new section 174A for tax years beginning after December 31, 2021, by amending their tax returns or treating it as a change in method of accounting.

Another special transition rule would allow all taxpayers that paid or incurred domestic research or experimental expenditures after December 31, 2021, and before January 1, 2025, to elect to deduct the remaining unamortized balance of the capitalized domestic research or experimental expenditures either over a one or two tax year period beginning after December 31, 2024.

Modification of limitation on business interest: The Finance Committee proposal makes permanent the calculation of adjusted taxable income that corresponds with earnings before interest, taxes, depreciation, and amortization (EBITDA) for the purposes of calculating the deduction limits for net business interest expense. Similar to the House-passed bill, the Finance Committee proposal also amended the floor plan financing exception to permanently expand the definition of "motor vehicle" to include any trailer or camper designed to provide temporary living accommodations for recreational, camping or seasonal use, and designed to be towed by a motor vehicle. The changes would apply to taxable years beginning after December 31, 2024.

The Finance Committee proposal would add a provision to section 163(j) to provide that the interest limitation applies to business interest regardless of whether the taxpayer would otherwise deduct such business interest or capitalize such business interest under an interest capitalization provision. The amount allowed as business interest expense after applying section 163(j)'s interest limitation provision would be applied first to the capitalized business interest. The provision would not, however, apply to interest capitalized under section 263(g) or 263A(f). The changes would apply to taxable years beginning after December 31, 2025.

Limitation on excess business losses on non-corporate taxpayers: Under current law, excess business losses of noncorporate taxpayers are disallowed and carried forward as a net operating loss in the subsequent tax year. While the excess business loss limitation is set to expire for tax years beginning on or after January 1, 2029, the House-passed bill would permanently extend the limitation on excess business losses for noncorporate taxpayers. Further, if enacted, this provision would cause excess business losses disallowed in tax years beginning after December 31, 2024, to be includible in the taxpayer's computation of excess business losses in subsequent years. Effectively this would limit the amount of trade or business losses (including amounts carried forward as an NOL) that may offset non-trade or business income in tax years beginning after December 31, 2025.

The Finance Committee proposal is substantively similar to the House-passed bill, with a few modifications. Specifically, the Finance Committee proposal addresses several ancillary issues such as the treatment of loss carryovers upon termination of an estate or trust, the treatment of excess business loss carryovers with respect to discharge of indebtedness, and the treatment of net business loss carryovers in the context of an individual's title 11 case. It further provides the Secretary broad regulatory authority to prescribe regulations or guidance to carry out section 461(l), including defining the scope of gross income and deductions attributable to a trade or business and providing rules in the case of a termination of a trust or estate.

With respect to excess business losses upon termination of an estate or trust, the Finance Committee proposal would transfer the carryover to the beneficiary succeeding the trust or estate. However, such beneficiary would be subject to the excess business loss rules on such carryovers (*i.e.*, the beneficiary would be required to include the disallowed loss as a business deduction arising in the succeeding taxable year).

The modifications to excess business losses are generally effective retroactively to losses arising in taxable years beginning after December 31, 2024. Otherwise, the modification to make excess business losses permanent is effective for taxable years beginning after December 31, 2026.

Treatment of certain qualified sound recording productions: The Finance Committee proposal is consistent with the House-passed bill. The Finance Committee's proposed language would amend section 181 to expand the expensing rules for qualified film, television, and live theatrical productions to include qualified sound recording productions. The changes would allow a taxpayer to elect to deduct up to $150,000 of the aggregate cost of any qualified sound recording production or the cumulative cost of all such qualified sound recording production in the taxable year incurred if such production commences before January 1, 2026. The changes would provide that a qualified sound recording production" is defined as a sound recording (as defined in 17 USC. sec. 101) produced and recorded in the US

Additionally, the Finance Committee proposal would modify section 168(k) to include qualified sound recording productions placed in service before January 1, 2029, as qualified property eligible for bonus depreciation. A qualified sound recording production is placed in service at the time of initial release or broadcast.

The changes would apply to productions commencing in taxable years ending after the date of enactment.

Employee retention tax credits: The Finance Committee proposal would make several changes to COVID-related employee retention tax credits (ERTC), including potential penalties applicable to ERTC promoters, disallowance of certain refunds claimed after January 31, 2024, and extension of the statute of limitations applicable to certain ERTC claims.

Further, under the proposal, ERTC promoters would be required to comply with certain due diligence requirements related to ERTC claims and would be subject to a penalty of $1,000 for each failure to comply. ERTC promoters would include any person who provides aid, assistance, or advice related to ERTC claims who:

- Charges or receives fees based on the amount of ERTC claims and whose gross receipts from such aid, assistance, or advice exceeds 20 percent of gross receipts for the taxable year, or
- Whose aggregate gross receipts from such aid, assistance, or advice for the taxable year or preceding taxable:
    - Exceeds 50 percent of gross receipts for the taxable year, or
    - Exceeds $500,000 and exceeds 20 percent of gross receipts for the taxable year.

Certified professional employer organizations would not be treated as ERTC promoters. Upon enactment, refunds claimed for Q3 2021 after January 31, 2024, would be disallowed.

Further, the assessment statute of limitations on ERTC claims for Q3 2021 would be extended until six years from the later of:

- The date of filing of the original quarterly return,
- April 15th of the year following the end of the calendar year, and
- The date the ERTC claim was made.

Taxpayers would also be allowed to file a refund claim for any amount attributable to a deduction for improperly claimed Q3 2021 ERTC wages until the end of the same six year assessment statute.

Expansion of section 162(m) limits on deductions of certain executive compensation to controlled group: This Finance Committee proposal closely follows the House-passed bill and would provide, similar to the House version, that effective for taxable years beginning after December 31, 2025, in the case of a publicly held corporation that is a member of a controlled group, payments made by all members of the controlled group are aggregated to determine the deduction disallowance. Under the proposal, payments to "specified covered employees" made by any member of the controlled group would be aggregated and if the aggregate amount exceeds $1 million, then the deduction limitation for any amounts paid in excess of $1 million would be allocated pro rata to each member of the controlled group, based on the percentage of total compensation paid by each member of the controlled group.

A "specified covered employee" with respect to the controlled group means the principal executive officer, principal financial officer, and any "once covered, always covered" employees of the publicly held corporation member of the controlled group. In addition, a "specified covered employee," for taxable years beginning after

December 31, 2026, includes any employee that is among the 5 highest compensated employees for the taxable year, taking in account all members of the controlled group. The controlled group is determined under sections 414(b), (c), (m), and (o), which generally set forth rules for treating entities as a single employer for employee benefit purposes.

Enhancement of employer-provided child-care credit: The Senate Finance Committee's tax proposed revisions to section 45F are the same as the provisions in the House-passed bill and would apply to amounts paid or incurred after December 31, 2025. Under these amendments, the credit amount determined under section 45F would be increased to a maximum allowable credit of $500,000 instead of $150,000 ($600,000 in the case of an eligible small business), subject to an inflation adjustment.

Extension and enhancement of paid family and medical leave credit: The Finance Committee's proposals to section 45S are the same as the provisions in the House-passed bill and would make the credit permanent, applying enhancements to the credit to taxable years beginning after December 31, 2025. Under these enhancements, the credit amount determined under section 45S is equal to either the applicable percentage of the amount of wages paid to qualifying employees with respect to any period in which such employees are on family and medical leave, or if such employer has an insurance policy with regards to the provision of paid family and medical leave which is in force during the taxable year, the applicable percentage of the total premiums paid or incurred by such employer during the taxable year with respect to the policy. The employer can elect which amount to use. The other enhancements to section 45S included in the committee's tax proposal would include modifications to the aggregation rule, the treatment of benefits mandated or paid for by state or local governments, and section 280C.

Increased Taxable REIT Subsidiary Asset Test Threshold: Under current law, a real estate investment trust ("REIT") may not own securities of one or more taxable REIT subsidiaries representing more than 20 percent of the REIT's assets at the end of each calendar quarter. The House-passed bill would increase that threshold to 25 percent and apply to taxable years beginning after December 31, 2025, however, no companion provision was included in the Senate Finance Committee's release of its version of the reconciliation package.

Payments from partnerships to partners for property and services: Section 707(a)(2) provides that "[u]nder regulations prescribed by the Secretary," certain transactions between a partner and a partnership (or 2 or more partners) are treated as occurring between the partnership and a person who is not a partner (or 2 or more partners acting other than in their capacity as partners). The Finance Committee's proposal would clarify section 707(a)(2) and replace "Under regulations prescribed by the Secretary" with "Except as provided by the Secretary" as the introduction to the section 707(a)(2) rules.

Third party litigation funding reform: The Finance Committee's proposal includes new provisions intended to prevent investors from financing litigations involving third parties and receiving a share of the litigation proceeds under a financing agreement or derivative contract as long-term capital gains (in the case of domestic investors) or as amounts exempt from withholding tax (in the case of foreign investors). The provisions generally would exclude litigation financing agreements from treatment as capital assets and exclude litigation financing proceeds from gross income for income tax purposes. Instead, the bill would impose on the litigation funder's realized gains on the financing an excise tax equal to the highest individual income tax rate plus 3.8 percent. The excise tax would be imposed at the entity level in the case of a partnership, S corporation or other pass-through entity that receives litigation proceeds pursuant to a litigation financing agreement. Parties to the litigation, or law firms affiliated with the litigation, who enter into litigation financing agreements would be required to withhold 50 percent of the excise tax rate from proceeds paid to the funders under the financing agreements. These provisions would not apply to loan agreements meeting certain requirements. These changes would apply to taxable years beginning after December 31, 2025.

Intangible drilling and development costs taken into account for purposes of computing adjusted financial statement income: Section 55(a) generally imposes a tax equal to the excess (if any) of – (1) the tentative minimum tax for the taxable year, over (2) the regular tax for the taxable year plus the tax imposed by section 59A. In the case of an applicable corporation, the tentative minimum tax for the taxable year is the excess of – (i) 15 percent of the adjusted financial statement income ("AFSI") for the taxable year (as determined under section 56A), over (ii) the corporate AMT foreign tax credit for the taxable year. Section 56A(a) generally provides that the term "adjusted financial statement income" means, with respect to any corporation for any taxable year, the net income or loss of the taxpayer set forth on the taxpayer's applicable financial statement for such taxable year, adjusted as provided in this section. Section 56A(c) currently provides the general adjustments to AFSI. The Finance Committee tax language would propose to include an additional adjustment to AFSI for any deduction allowed for intangible drilling and development costs for oil and gas wells and geothermal wells under section 263(c) to the extent of the amount allowed as deductions in computing taxable income for the year. Correspondingly, the AFSI adjustment would disregard any amount of depletion expense that is taken into account on its applicable financial statement with respect to the intangible drilling and development costs of such property. The amendments apply to taxable years beginning after December 31, 2025.

Enhancement of Advanced Manufacturing Investment Credit (48D): The Finance Committee's proposal would amend section 48D by increasing the advanced manufacturing investment credit to 30 percent from 25 percent of the qualified investment for any taxable year with respect to any advanced manufacturing facility of an eligible taxpayer. This amendment and increase of the section 48D credit is proposed to apply to property placed in service after December 31, 2025. Additionally, the committee bill would replace the term "foreign entity of concern" as defined in the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, with "specified foreign entity (as defined in section 7701(a)(51))."

Permanent enhancement of low-income housing tax credit: The Finance Committee's proposal would permanently increase the state housing credit ceiling for allocation of the 9 percent low-income housing tax credit ("LIHTC") by 12 percent for calendar years after 2025. It would also increase the availability of the 4 percent LIHTC for projects financed with tax-exempt private activity bonds by reducing the tax-exempt bond financing threshold from at least 50 percent of the aggregate basis of the building and land to 25 percent for tax-exempt private activity bonds issued beginning in 2026.

Depreciation

This section outlines the key depreciation provisions, detailing the methods and timelines through which businesses can systematically allocate the cost of their assets over their useful lives.

Full expensing for certain business property: Section 168(k) provides an additional first-year depreciation allowance (commonly referred to as "bonus depreciation") for qualified property, the deduction for which is equal to the applicable percentage of the qualified property's adjusted basis. For qualified property placed in service after September 27, 2017, and before January 1, 2023, or January 1, 2024, for property with longer production periods and plants bearing fruits and nuts ("specified plants"), the applicable percentage is equal to 100 percent, with a 20 percent phase down for each year thereafter.

Different from the House-passed bill that reinstated 100 percent bonus depreciation for qualified property acquired and placed in service after January 19, 2025, and before January 1, 2030 (or January 1, 2031, for property with longer production periods), the Finance Committee proposal would amend section 168(k) to permanently reinstate 100 percent bonus depreciation for qualified property acquired and placed in service after January 19, 2025.

It would also amend section 168(k)(10) to provide a transitional election to apply 40 or 60 percent bonus depreciation on certain property placed in service during the first taxable year ending after January 19, 2025.

Increased dollar limitations for expensing of certain depreciable business assets: The Finance Committee proposal is consistent with the House-passed bill. The proposal would amend sections 179(b)(1) and (2) to increase the dollar limitation to $2.5 million and the phaseout threshold to $4 million. These amounts are indexed for inflation in taxable years beginning after 2025 and would apply to property placed in service in taxable years beginning after December 31, 2024.

Special Depreciation Allowance for Qualified Production Property: Section 168(k) provides bonus depreciation for qualified property acquired or self-constructed and placed in service after September 27, 2017, and before January 1, 2028, or January 1, 2029, for property with longer production periods and specified plants. Specifically, section 168(k)(2)(A) generally defines "qualified property" as MACRS property that has a recovery period of 20 years or less, computer software as defined in and depreciated under section 167(f)(1), water utility property as defined in section 168(e)(5), qualified film or television production as defined in section 181(d), and qualified live theatrical production as defined in section 181(e). Nonresidential real property is not qualified property for purposes of bonus depreciation because section 168(e)(2)(B) defines "nonresidential real property" as section 1250 property that is not residential rental property or property with a class life less than 27.5 years, has a recovery period of 39 years, and thus, is not qualified property for bonus depreciation.

Nearly identical to the House-passed bill, the Finance Committee proposal would amend section 168 to add new section 168(n) that allows a taxpayer to elect to apply 100-percent bonus depreciation to qualified production property. New section 168(n)(2)(A) generally defines "qualified production property" as the portion of any nonresidential real property used by the taxpayer as an integral part of a qualified production activity, the original use commences with the taxpayer, the construction of such property begins after January 19, 2025 and before January 1, 2029, and is placed in service in the United States or any possession thereof before January 1, 2031 – in contrast to the House-passed bill that required a placed in service date before January 1, 2033. In the case of property with respect to which a taxpayer is a lessor, property used by a lessee is not considered to be used by the taxpayer as part of a qualified production activity.

Termination of cost recovery for qualified clean energy facilities, property and technology: The Finance Committee proposes to strike section 168(e)(3)(B)(viii) which would remove 5-year property classification for any qualified facility under section 45Y and qualified property or energy storage technology under section 48E. This amendment is proposed to apply to property placed in service after the date of enactment of the bill.

Energy Credits

Restrictions Related to Prohibited Foreign Entities (Sections 48E, 45Y, 45X, 45Q, 45U, and 45Z): The House bill proposed to add certain restrictions and prohibitions related to foreign entities for taxpayers intending to claim credits under sections 48E, 45Y, 45X, 45Q, 45U, 45Z and certain geothermal heat pump property as described in section 48(a)(3)(A)(iii). Additionally, the House-passed bill restricted taxpayers who receive material assistance from "prohibited foreign entities" from accessing certain credits beginning one year after the date of enactment of the proposed bill. The bill would add section 7701(a)(51), which defines a "prohibited foreign entity" as (i) a specified foreign entity or (ii) a foreign influenced entity and section 7701(a)(52), which defines "material assistance from a prohibited foreign entity."

The Finance Committee proposal would retain the general framework of these restrictions and prohibitions but substantially modifies the definition of "prohibited foreign entity," in particular with respect to a "foreign influenced entity," and the application of material assistance.

While retaining main portions of the prohibited foreign entity restriction, the Senate bill differs in its application to the credits as follows:

- Specified foreign entity:
    - For section 45Y, 48E, 45Q, 45X, and 45Z, no credit is determined with respect to a specified foreign entity for any taxable year beginning after the date of enactment of the bill,
- Foreign influenced entity:
    - For section 45Y, 45U, 45X, and 45Z, no credit is determined with respect to a foreign-influenced entity for any taxable year beginning 2 years after the date of enactment of the bill.
    - For section 48E and 45Q, the foreign influenced entity restriction applies for any taxable year beginning after the date of enactment of the bill.
    - For section 45Q, 45U, 45Z, the "effective control" (described below) is disregarded in determining whether the taxpayer is a foreign influenced entity.

- Material assistance from prohibited foreign entities apply to qualified facilities or energy storage technology ("EST") under section 45Y or 48E that begin construction after December 31, 2025, and to eligible components under section 45X for any taxable year beginning after the date of enactment.

Specified Foreign Entity

Similar to the House-passed bill, the Finance Committee proposal proposes to define "specified foreign entity" as any of the following:

i. A foreign entity of concern described in subparagraph (A), (B), (D), or (E) of section 9901(8) of the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021,
ii. An entity identified as a Chinese military company operating in the United States in accordance with section 1260H of the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021,
iii. An entity included on a list required by clause (i), (ii), (iv), or (v) section 2(d)(2)(B) of Public Law 117-78,
iv. An entity specified under section 154(b) of the National Defense Authorization Act for Fiscal Year 2024, or
v. A foreign-controlled entity.

Foreign-Influenced Entity

The committee bill would substantially modify the definition of "foreign influenced entity" as an entity:

i. With respect to which, during the taxable year,
    a. A specified foreign entity has the direct or indirect authority to appoint a covered officer of such entity,
    b. A single specified foreign entity owns at least 25 percent, or multiple specified foreign entities own in the aggregate 40 percent of such entity, or
    c. At least 40 percent of the debt of such entity is held in the aggregate by one or more specified foreign entities, or
ii. Which, during the previous taxable year, made a payment to a specified foreign entity pursuant to a contract, agreement, or other arrangement that entitles such specified foreign entity to exercise effective control over
    a. Taxpayer's qualified facility or energy storage technology (EST) for purposes of section 45Y or 48E, or
    b. With respect to eligible component produced by the taxpayer for purposes of section 45X, the extraction, processing, or recycling of any applicable critical mineral or production of other eligible component.

The Senate bill increases from the House-passed levels, the ownership threshold described above in i.b. from 10 percent and 25 percent to 25 percent and 40 percent, respectively. The Finance Committee proposal would also increase the debt percentage from 25 percent to 40 percent.

The Finance Committee proposal would replace the FDAP (fixed, determinable, annual, or periodical) payment included in the House-passed bill (*i.e.*, foreign influenced entity includes an entity that makes certain percentage of its total fixed, determinable, annual or periodic payments to a specified foreign entity) with "effective control" as described above. Furthermore, the "effective control" prong of the foreign influenced entity definition applies only for purposes of sections 45Y, 45X, and 48E. The term "effective control" means an agreement or arrangement which provides contractual counterparties of a taxpayer with specific authority over key aspects of the production of eligible components, energy generation, or energy storage.

The Finance Committee proposal would direct Treasury, in consultation with the Secretary of Energy, to issue guidance as necessary to carry out the purposes of the foreign influenced entity restrictions, including establishing rules to prevent entities from evading, circumventing, or abusing such restriction. Until such guidance is issued, the Finance Committee proposal would provide that the term "effective control" means an unrestricted contractual right of a contractual counterparty to:

i. Determine the quantity or timing of production of an eligible component,
ii. Determine the amount or timing of activities related to the production of electricity or the storage or energy,
iii. Determine which entity may purchase or use the eligible component,
iv. Determine which entity may purchase or use the output of a qualified facility,
v. Restrict access to data critical to production or energy storage, or to the site of production or any part of a qualified facility or energy storage, to the personnel or agents of such contractual counterparty, or
vi. Exclusively maintain, repair, or operate any plant or equipment necessary to the production by the taxpayer.

With respect to any licensing agreement for intellectual property or other arrangement related to a qualified facility, energy storage, or production of an eligible component, "effective control" could include additional contractual rights such as, among others, rights retained to direct sourcing of components, subcomponents or applicable critical minerals, rights retained to direct the operation of any qualified facility, energy storage, or any production unit, and rights retained to limit the taxpayer's utilization of intellectual property. The effective control related to any licensing agreement or other arrangement would not apply in the case of a bona fide purchase or sale of intellectual property.

Material assistance from a prohibited foreign entity

The House-passed bill defined "material assistance from a prohibited foreign entity" as any component, subcomponent, or applicable critical minerals (as defined in section 45X(c)(6)) included in any property that is extracted, processed, recycled, manufactured, or assembled by a prohibited foreign entity, or any design of such property which is based on any copyright or patent held by a prohibited foreign entity or any know-how or trade secret provided by a prohibited foreign entity.

Substantially modifying this definition, the Finance Committee proposal would define "material assistance from a prohibited foreign entity" as a material assistance cost ratio which is less than the threshold percentage based on the applicable calendar year. Specifically, the taxpayer's direct materials cost of manufactured products incorporated into a qualified facility or EST, or components, subcomponents, or constituent materials used in an eligible component that are attributable to a non-prohibited foreign entity must not be less than the threshold percentage. The allowable percentage of non-prohibited foreign entity components in qualified facilities and EST under sections 45Y and 48E increases incrementally each year.

Those threshold percentages are as follows:

- For a qualified facility or EST the construction of which begins in 2026, 40 percent,
- For a qualified facility or EST the construction of which begins in 2027, 45 percent
- For a qualified facility or EST the construction of which begins in 2028, 50 percent
- For a qualified facility or EST the construction of which begins in 2029, 55 percent, and
- For a qualified facility or EST the construction of which begins after 2029, 60 percent.

The threshold percentages for eligible components under section 45X are as follows:

Calendar year of production	Solar components	Wind components	Inverter components	Battery components	Critical mineral components
2026	50%	85%	50%	60%	0%
2027	60%	90%	55%	65%	0%
2028	70%		60%	70%	0%
2029	80%		65%	80%	0%
2029	85%		70%	85%	0%
2030	85%		70%	85%	25%
2031	85%		70%	85%	30%
2032	85%		70%	85%	40%
After 2032					50%

The "material assistance cost ratio" with respect to a qualified facility or EST under section 45Y and 48E is determined as an amount equal to (a) the taxpayer's total costs for all manufactured products which are incorporated into the qualified facility or EST upon completion of construction minus (b) the taxpayer's total costs for such manufactured products that are mined, produced, or manufactured by a prohibited foreign entity, divided by the total costs in (a).

Similarly, the material assistance cost ratio with respect to an eligible component under section 45X is determined as an amount equal to (a) the taxpayer's total direct materials costs that are paid or incurred for production of such eligible component minus (b) the taxpayer's total direct materials costs paid or incurred for production of such eligible component that are attributable to a prohibited foreign entity, divided by the total direct materials costs in (a).

The term "manufactured product" has the same meaning as in IRS Notice 2023-38.

The Finance Committee proposal would direct Treasury, in consultation with the Secretary of Energy, to issue safe harbor tables that identify the percentage of the total direct material costs of any manufactured product or eligible component which is attributable to a prohibited foreign entity. Until the guidance is issued, and for construction of a qualified facility which begins on or before the date that is 60 days after the date of issuance of such tables, a taxpayer may use the safe harbor tables included in Notice 2025-08 and rely on a certification by the supplier ("supplier certification") of the manufactured product, eligible components, or constituent element, materials, or subcomponent of an eligible component of the total direct material costs that was not produced or manufactured by a prohibited foreign entity.

The Finance Committee proposal contains an exclusion, allowing a taxpayer to elect to disregard the cost to the taxpayer with respect to any manufactured product, eligible component, or constituent element, material, or subcomponents of an eligible component which is acquired pursuant to a binding written contract entered into prior to June 16, 2025, and placed in service (or used in a product sold) before January 1, 2030.

Penalties relating to the material assistance cost ratio

The Finance Committee proposed to amend section 6662 to provide that with respect to any disallowance of credit under sections 45X, 45Y, or 48E (including such credits elected under section 6417) by reason of overstating the material assistance cost ratio, a substantial understatement of income tax occurs if the amount of the understatement of the tax year exceeds the greater of 1 percent of the tax required to be on the return or $5,000. Current law provides the greater of 10 percent of the tax required to be on the return or $5,000 to be considered substantial understatement of tax.

The Finance Committee proposal also proposed to add a new section 6695B, which would impose penalties on any supplier that provides a supplier certification that is inaccurate or false, which resulted in the disallowance of the credits under section 45Y, 48E, and 45X and an understatement of income tax for the taxable year in an amount exceeding the lesser of 5 percent of tax required to be shown on the return or $100,000. The penalty amount would equal the greater of 10 percent of the amount of underpayment attributable to the inaccuracy or $5,000. No penalty is imposed if any inaccuracy or falsity is due to a reasonable cause and not willful neglect.

Transferability

The Finance Committee proposed to add a new subsection (g) under section 6418 to prohibit an eligible taxpayer from transferring any portion of the credits determined under sections 45Q, 45U, 45X, 45Y, 45Z, and 48E to a specified foreign entity as defined in section 7701(a)(51)(B).

Extension and modification of clean fuel production credit: The Senate Finance Committee bill would extend section 45Z to apply to fuel produced and sold before December 31, 2031, but unlike the House bill, the committee bill would leave intact transferability under section 6418 for fuel produced and sold after December 31, 2027. Under the House-passed bill, fuel sold after December 31, 2025, must be exclusively derived from a feedstock produced or grown in the United States, Mexico, or Canada to be eligible for the section 45Z credit.

For fuel produced and sold after December 31, 2025, the Finance Committee proposal would provide a formula to proportionately reduce the amount of the section 45Z credit based on the foreign feedstock percentage used to produce transportation fuel during the taxable year. The Finance Committee proposal would require the Secretary to issue guidance regarding implementation of the reduction to the credit for use of foreign feedstocks by December 31, 2025.

The Finance Committee proposal would continue to permit taxpayers to calculate the section 45Z credit based on their fuel's emission rate. Under current law, if the emission rate is less than zero, they can currently claim a credit in excess of $1.00 per gallon. However, by prohibiting negative emissions rates, the 45Z credit would be capped at $1 per gallon/gallon equivalent, or $1.75 for SAF (but this bill also gets rid of the increased rate for SAF and caps all 45Z credits at $1/gallon). It contains similar modifications to the determination of emissions rates for taxable years beginning after December 31, 2025, that the House bill contained; specifically, the committee bill would also provide that the lifecycle greenhouse gas emissions shall be adjusted to exclude any emissions attributed to indirect land use change. Additionally, despite the Finance Committee bill's general prohibition of negative emissions rates for transportation fuels, the bill provides that the Secretary may provide a distinct emissions rate that is less than zero for specific feedstocks used to produce transportation fuel, which may include dairy manure, swine manure, poultry manure, or other sources determined appropriate by the Secretary.

The definition of the term "transportation fuel" is also updated in the Finance Committee proposal to prevent double credits, providing that transportation fuel does not include a fuel that is produced from a fuel for which a section 45Z credit is allowable. The Finance Committee proposal would also amend section 45Z(f)(3) to provide the Secretary with authority to prescribe additional related person rules for entities that are not already described in the provision.

The Finance Committee proposal would eliminate the increased credit amount specific to sustainable aviation fuel (SAF), effective for fuel produced after December 31, 2025. Additionally, it would add a new coordination provision for SAF, providing that for SAF sold after December 31, 2024, and before October 1, 2025, the amount of the section 45Z credit shall be reduced by an amount equal to the amount of the SAF credit calculated under section 6426(k)(1) (the SAF blending credit), as if such subsection applied with respect to such gallon of fuel. The bill also amends section 6426(k) to provide that the SAF blending credit shall not apply to any sale or use for any period after September 30, 2025.

Finally, the Finance Committee proposes the same restrictions as the House bill related to prohibited foreign entities with modifications to the definition of "prohibited foreign entity."

Restriction on the extension of advanced energy project credit program (48C): The Finance Committee proposal would amend section 48C by modifying language related to the period of issuance, which currently allows credit amounts allocated to projects that have their certification revoked to increase the total credit allocation limit of $10 billion and potentially be reallocated under the section 48C Program. It would also prevent any credit already allocated from ever being reallocated by disallowing an increase to the credit allocation limit of $10,000,000,000 due to the revocation of a project's certification. Because the full

$10,000,000,000 has been allocated to date, this amendment would prevent any future allocation rounds under section 48C.

Termination of previously owned clean vehicles credit: The House-passed bill proposed to terminate the section 25E credit with respect to any vehicle acquired after December 31, 2025. The Finance Committee proposal would amend this to terminate the credit with respect to any vehicles acquired after 90 days from the date of enactment of the bill.

Termination of clean vehicle credit: The House-passed bill proposed to terminate the section 30D credit with respect to any vehicle placed in service after December 31, 2026. The House-passed bill also would provide a manufacturer-specific sales limitation for taxable year 2026, so that any vehicle placed in service after December 31, 2025, would not be treated as a new clean vehicle if, during the period beginning on December 31, 2009, and ending on December 31, 2025, the manufacturer of such vehicle sold more than 200,000 covered vehicles (*i.e.*, new qualified plug-in electric drive motor vehicles and new clean vehicles) for use in the United States. It would also add controlled group rules similar to those in section 30B(f)(4) for purposes of the special rule for taxable year 2026. The Finance Committee proposal would terminate the section 30D credit for vehicles acquired more than 180 days after the date of enactment. Unlike the House-passed bill, the committee bill would not provide a manufacturer-specific sales limitation for taxable year 2026.

Modification and termination of qualified commercial clean vehicle credit: The Finance Committee proposal would terminate the section 45W credit with respect to any vehicle acquired after the date that is 180 days after enactment of the bill.

The Finance Committee proposal would also modify the section 45W credit for vehicles acquired after June 16, 2025, by adding new requirements. Specifically, to qualify for the credit, vehicles acquired after June 16, 2025, must have final assembly that occurs within North America, and vehicles with gross vehicle weight rating of less than 14,000 pounds are subject to the manufacturer's suggested retail price limitation that is imposed in section 30D. The proposal would also exclude certain vehicles that have a gross vehicle weight rating of less than 14,000 pounds from being considered qualified commercial clean vehicles if certain foreign entity of concern restrictions under section 30D(d)(7)(A) or (B) and critical minerals and battery components requirements under section 30D(e)(1)(A) or (2)(A) are not satisfied.

Termination of alternative fuel vehicle refueling property credit: The House-passed bill proposed to terminate the section 30C credit with respect to alternative fuel vehicle refueling property placed in service after December 31, 2025. The Finance Committee proposal proposes to terminate the credit with respect to alternative fuel vehicle refueling property placed in service on a date which is 12 months after the date of enactment of the bill.

Termination of energy efficient home improvement credit: The House-passed bill would terminate the section 25C credit with respect to property placed in service after December 31, 2025. The Finance Committee proposal would terminate the section 25C credit with respect to property placed in service more than 180 days after the date of enactment.

Termination of residential clean energy credit: The House-passed bill would terminate the section 25D credit with respect to property placed in service after December 31, 2025. The Finance Committee proposal would terminate the section 25D credit with respect to expenditures made more than 180 days after the date of enactment of the bill.

Termination of new energy efficient home credit: The House-passed bill proposed to terminate the new energy efficient home credit under section 45L for any qualified new energy efficient homes acquired after December 31, 2025 (or December 31, 2026, in the case of any home for which construction began before May 12, 2025). The Finance Committee proposal would amend section 45L and terminates the new energy efficient home credit for any qualified new energy efficient home acquired after the date that is 12 months after the enactment of the bill.

Phase-out and restrictions on clean electricity production credit: The House-passed bill proposed to terminate the section 45Y credit for qualified facilities that (a) begin construction more than 60 days after the bill's enactment or (b) are placed in service after 2028, with the exception of nuclear facilities. The Finance Committee proposal does not retain this early termination but instead provides accelerated phase-out percentages for wind and solar qualified facilities. Specifically, for wind and solar qualified facilities, the amount of the section 45Y credit otherwise determined would be as follows: (1) 60 percent of the credit for facilities that begin construction in calendar year 2026; (2) 20 percent of the credit for facilities that begin construction in calendar year 2027; and (3) no credit is available for facilities that begin construction after 2027.

Similar to the House-passed bill, the Finance Committee proposal would deny the section 45Y credit for taxable years beginning after the date of enactment with respect to any electricity production using certain property described in section 25D (*i.e.*, solar water heating property, solar electric property and small wind property) that is leased or rented to a third party for use at a dwelling unit or residence of such third party.

For all other qualifying technologies, such as nuclear, geothermal, and hydropower, the section 45Y credit would continue to be available under the Finance Committee proposal. The termination of the section 45Y in reference to the greenhouse gas emissions rate not greater than 25 percent level of 2022 is proposed to be stricken.

The Finance Committee proposal provides that whether the expansion of facility and incremental production under section 45Y(b)(1)(C) results in the additions of capacity of the facility may be determined in any reasonable manner, including based on: determinations by the Federal Energy Regulatory Commission, the Nuclear Regulatory Commission, or any similar entity; determinations by an independent professional engineer; reports to or issued by regional transmission organizations or other operators; or any other method provided by the Secretary.

In addition, it includes similar prohibitions and restrictions as provided in the House bill, impacting taxpayers who are prohibited foreign entities or who receive material assistance from prohibited foreign entities (as defined in section 7701(a)(52)). However, as further discussed in a separate section, the Senate bill substantially modifies the definition of prohibited foreign entities and material assistance from prohibited foreign entities.

Further, the Finance Committee proposal would eliminate the statutory exceptions to the phaseout for elective payment for facilities with a maximum net output of at least 1 megawatt that fail to satisfy the domestic content requirement.

Finally, it would amend section 45Y(b)(2)(C) to add, that for purposes of determining the greenhouse gas emissions rates for types and categories of facilities, the Secretary must also consider studies, published on or before the date of enactment, which demonstrate a net lifecycle greenhouse gas emissions rate which is less than zero, using widely accepted lifecycle assessment standards, such as standards developed by the International Organization for Standardization.

Phase-out and restrictions on clean electricity investment credit: The House-passed bill proposed to terminate the section 48E credit for facilities that (a) begin construction more than 60 days after the bill's enactment or (b) are placed in service after 2028. The Finance Committee bill does not retain this termination but would instead amend section 48E by providing accelerated phase-out percentages rules for solar and wind facilities. Specifically, for wind and solar qualified facilities, the amount of the section 48E credit otherwise determined is as follows: (1) 60 percent of the credit for facilities that begin construction in calendar year 2026; (2) 20 percent of the credit for facilities that begin construction in calendar year 2027; and (3) no credit is available for facilities that begin construction after 2027. The specific phase out for wind and solar qualified facilities does not apply to energy storage technology which is placed in service at a qualified wind or solar facility.

Similar to the House-passed bill, the Finance Committee proposal would deny the section 48E credit for taxable years beginning after the date of enactment with respect to any electricity production using certain property described in section 25D (*i.e.*, solar water heating property, solar electric property and small wind property) that is leased or rented to a third party for use at a dwelling unit or residence of such third party.

For all other qualifying technologies, such as nuclear, geothermal, and hydropower and energy storage technology, the section 48E credit would continue to be available under the Finance Committee proposal by incorporating the phase-out rule as provided under section 45Y.

The Finance Committee proposal includes similar prohibitions and restrictions as provided in the House bill, impacting taxpayers who are prohibited foreign entities or who receive material assistance from prohibited foreign entities (as defined in section 7701(a)(52)). However, as further discussed below in a separate section, the Senate bill substantially modifies the definition of prohibited foreign entities and material assistance from prohibited foreign entities.

In addition, the Finance Committee proposal would maintain modifications to certain recapture provisions under 50(a) as proposed in the House-passed bill, retaining certain restrictions related to payments made by taxpayers to a specified foreign entity which entitles such specified foreign entity to exercise effective control.

Finally, the Finance Committee proposal would propose to increase the adjusted percentage for section 48E for purposes of qualifying for the domestic content bonus credit amount to 45 percent if construction begins on or after June 16, 2025, but before January 1, 2026 (27.5 percent for offshore wind), to 50 percent if construction begins during calendar year 2026 (35 percent for offshore wind), and to 55 percent if construction begins after 2026. Further, the Finance Committee proposal would eliminate the statutory exceptions to the phaseout for elective payment for facilities with a maximum net output of at least 1 megawatt that fail to satisfy the domestic content requirement.

Restrictions on carbon oxide sequestration credit: The Finance Committee proposal would amend section 45Q for facilities or equipment placed in service after December 31, 2022, by increasing the credit rate for the utilization of qualified carbon oxide in taxable years beginning after 2025. The committee's increased credit rate for utilization would equal the rate for qualified carbon oxide that is disposed of in secure geological storage without prior utilization.

Phase-out and restrictions on zero-emission nuclear power production credit: The House-passed bill proposed to terminate section 45U for taxable years beginning after 2031 and to restrict prohibited foreign entities from claiming the credit. The Finance Committee proposal would not terminate the credit earlier than under current law. As such, the provision remains set to expire for taxable years beginning after December 31, 2032. The Finance Committee proposal would also retain the restrictions related to prohibited foreign entities with modified definitions of such terms as described in other sections. The Finance Committee proposal would also introduce a requirement starting in taxable years beginning after 2027 that would restrict facilities from using certain imported nuclear fuel. Specifically, it provides that nuclear fuel used by a qualified nuclear power facility during a taxable year cannot be: (I) produced in a covered nation (*i.e.*, China, Iran, North Korea, and Russia) or by a covered entity (defined as an entity organized under the laws of, or otherwise subject to the jurisdiction of, the government of a covered nation); (II) exchanged with, traded for, or substituted for nuclear fuel described in (I); or (III) otherwise obtained in lieu of nuclear fuel described in (I) in a manner which is designed to circumvent the purposes of this restriction. A taxpayer must certify to the Secretary that any fuel used by such facility during a taxable year complies with the aforementioned requirements. Additionally, the Finance Committee proposal includes an exception to such rule for fuel purchased pursuant to a binding written contract in effect before January 1, 2023, if such binding written contract is not modified in any material respect on or after such date.

Termination of clean hydrogen production credit: Under current law, the section 45V credit is available beginning on January 1, 2023, for hydrogen produced during a 10-year period at a clean hydrogen production facility, the construction of which begins before January 1, 2033. Both the House-passed bill and the Senate Finance Committee proposal would terminate the credit for clean hydrogen production facilities, the construction of which begins after December 31, 2025.

Phase-out and restrictions on advanced manufacturing production credit: The House-passed bill proposed to amend section 45X by accelerating the phase out of the credit where eligible components sold after December 31, 2031, would not be eligible for the credit. This change was not adopted in the Senate bill, which keeps the phase out as in current law (*i.e.*, 25 precent of the credit for eligible components sold in calendar year 2032, and no credit for eligible components sold after December 31, 2032).

The House-passed bill also proposed to introduce a phase out for critical mineral eligible components similar to other types of eligible components. The Finance Committee proposal would retain a phase out for critical mineral eligible components. However, it moves back the phase out period and applies this based on when applicable critical minerals are *produced* instead of when they are *sold*: the phase out percentage is equal to 75 percent of the credit for critical minerals *produced* during calendar year 2031, 50 percent for critical minerals *produced* during calendar year 2032, 25 percent for critical minerals *produced* during calendar year 2033 (25 percent), and 0 percent for critical minerals *produced* after calendar year 2033. Further, the Finance Committee proposal would adopt the House-passed bill amendment to terminate the credit for wind energy components produced and sold after December 31, 2027.

The House-passed bill introduced two restrictions within the definition of "eligible components" under section 45X(c)(1) to exclude property which: (1) includes any material assistance from a prohibited foreign entity, or (2) is produced subject to a licensing agreement with a prohibited foreign entity for which the value of such agreement is in excess of $1,000,000. The Finance Committee proposal would retain only the first of these restrictions and amends the applicability date to taxable years beginning after the date of enactment of the bill (as compared to taxable years beginning two years after the enactment of the bill as proposed in the House-passed bill). Further, under the Finance Committee proposal, taxpayers that are prohibited foreign entities would not be eligible for a credit in taxable years beginning after the date of enactment of the bill. As discussed elsewhere in this section, the Finance Committee proposal would substantially modify the definitions of "prohibited foreign entities" and "material assistance." Notably, the committee bill did not adopt the House-passed bill's restrictions for taxpayers who have made payments to prohibited foreign entities that would have applied in taxable years beginning two years after the date of enactment.

In addition to the above, the Finance Committee proposal would remove the current rule allowing taxpayers to treat as having sold an eligible component to an unrelated person if such component is integrated, incorporated, or assembled into another eligible component that is sold to an unrelated person. Additionally, it would introduce in the definition of battery modules under section 45X(c)(5)(B)(iii) the requirement to be comprised of all other essential equipment needed for battery functionality, such as current collector assemblies and voltage sense harnesses.

Income from Hydrogen Storage, Carbon Capture, Advanced Nuclear, Hydropower, and Geothermal Energy Added to Qualifying Income of Certain Publicly Traded Partnerships Treated as Corporations (7704(d)(1)(E)): The House-passed bill proposed to amend section 7704(d)(1)(E) to add income from hydrogen storage and carbon capture to qualifying income of certain publicly traded partnerships treated as corporations. The Finance Committee bill would retain and extend the treatment of qualifying income to income derived from production of electricity from any advanced nuclear facility, production of electricity or thermal energy exclusively using geothermal energy or hydropower, and operation of geothermal energy or geothermal heat pump.

Summary of Modifications to Section 6418 Transferability: Various sections of the House-passed bill proposed to repeal certain credits from qualification as "eligible credits" and, therefore, the elective transfer under section 6418, with different effective dates. The Finance Committee proposal does not repeal credits from qualification as "eligible credits" and, therefore, the elective transfer rules continue to apply except for new restrictions imposed with respect transfers to certain foreign entities. Effectively, the Finance Committee proposal would restore transferability except for transfers to specified foreign entities.

Termination of Energy Efficient Commercial Buildings Deduction (179D): Under current law, section 179D allows a deduction for the cost of energy efficient commercial building property placed in service during the taxable year, subject to certain limitations. The section 179D deduction was made permanent by the Consolidated Appropriations Act of 2021 and was subsequently amended by the Inflation Reduction Act of 2022. The House-passed bill did not propose to amend section 179D, but the Finance Committee proposal would terminate the section 179D deduction with respect to property that begins construction more than 12 months after enactment of the bill.

Permanent renewal and enhancement of opportunity zones (1400Z-1)

The Finance Committee proposal would establish a permanent qualified opportunity zone (QOZ) program that builds off the version originally enacted in 2017 with several modifications. New QOZ designations would be made on a rolling ten-year basis beginning January 1, 2027, and would be effective on the "applicable start date", defined as the January 1 following the date on which such QOZ was certified and designated by the Treasury Secretary. QOZ designations will generally be made in the same manner as the process established under the Tax Cuts and Jobs Act, with certain modifications designed to narrow the range of census tracts eligible for designation by state CEOs by updating the definition of a low-income community (LIC) and eliminating the ability for contiguous tracts that are not LICs to be designated as QOZs. The LIC definition is modified so that only census tracts with a poverty rate of at least 20 percent or a median family income that does not exceed 70 percent (rather than 80 percent) of the applicable area median family income would be eligible for designation as QOZs and, for census tracts eligible for designation based on a 20-percent poverty rate, no census tract would be eligible for designation as a QOZ if the tract's median family income is at least 125 percent of the statewide median family income (or, in the case of metropolitan tracts, 125 percent of the metropolitan area median family income). At the same time, the modified LIC definition repeals the special rule in section 1400Z-1(b)(3) that exempted Puerto Rico from the general limitation imposed on all states, the District of Columbia, and other US possessions that no more than 25 percent of the jurisdiction's LICs could be designated as QOZ. This would significantly reduce the number of QOZs designated in Puerto Rico going forward.

The Finance Committee proposal generally would preserve the three taxpayer benefits achieved by making an investment in a qualified opportunity fund (QOF), at the taxpayer's election: (1) a temporary deferral of the capital gain reinvested in the qualified opportunity zone (the "rollover gain"); (2) a permanent 10 percent reduction (decreased from the maximum of 15 percent under the originally enacted QOZ program) in the amount of such gain that must be recognized if the investment is held for at least seven years; and (3) a permanent exclusion of future gains resulting from the investment in the opportunity zone if the investment is held for at least 10 years. The permanent exclusion of future gains resulting from the investment held for more than 30 years is capped at the fair market value of such investment on the date that is 30 years after the date of the investment. To qualify for these benefits, the rollover gain is generally required to be invested in the QOF during a 180-day period that begins on the date of the sale or exchange that generated the gain. The Finance Committee proposal also would modify the periods in which the permanent 10 percent reduction in the amount of such gain that must be recognized vests according to the following schedule at the conclusion of each year that the investment is held: Years 1-3 (1 percent); Years 4-5 (2 percent); and Year 6 (3 percent).

It also would establish additional taxpayer benefits for investments made in a newly defined “qualified rural opportunity fund.” For this purpose, a “qualified rural opportunity fund” is defined as a QOF that holds at least 90 percent of its assets in either (a) qualified opportunity zone business property (QOZBP) substantially all of the use of which, during substantially all of the QOF’s holding period, is in a rural QOZ, or (b) QOZ stock or a QOZ partnership interest in a QOZB (qualified opportunity zone business), substantially all of the tangible property owned or leased of which is QOZBP substantially all of the use of which is in a rural QOZ. The holder of an investment in a “qualified rural opportunity fund” also receives a permanent 30 percent reduction (rather than 10 percent) in the amount of such deferred gain that must be recognized if the investment is held for at least seven years following a modified vesting schedule at the conclusion of each year that the investment is held as follows: Years 1-3 (3 percent); Year 4-5 (6 percent); and Year 6 (9 percent).To further stimulate investments in rural QOZs, the bill provides a special rule that lowers the 100 percent substantial-improvement threshold for non-original use QOZBP owned by a QOZB (or QOF) to 50 percent in the case of tangible property located in a rural QOZ.

Lastly, the Finance Committee proposal would add certain reporting requirements for the QOZ program and provide funding to the IRS to carry out the reporting requirements.

International provisions

The House-passed bill includes several significant international tax provisions that build on the framework established by the TCJA. In addition, the proposal introduces a new enforcement mechanism – proposed section 899 – aimed at countering what some lawmakers view as discriminatory foreign tax regimes.

Modification of the Global Intangible Low-Taxed Income (“GILTI”) regime: The Finance Committee proposal would modify the GILTI regime to remove the reduction to GILTI related to a taxpayer’s qualified business asset investment (“QBAI”). As part of this change, it would require a taxpayer to include its net CFC tested income (“NCTI”) (rather than GILTI) in income.

It would also lower the percentage deductions related to a taxpayer’s NCTI inclusion and related section 78 gross-up to 40 percent for taxable years beginning after December 31, 2025. The current deduction related to GILTI is 50 percent and is currently scheduled to be reduced to 37.5 percent in 2026. When combined with the modifications to the foreign tax credit regime, this would generally result in an effective tax rate related to NCTI of 14 percent.

The Finance Committee proposal also would reduce the haircut for foreign income taxes deemed paid with respect to a NCTI inclusion from 20 to 10 percent. Stated differently, foreign income taxes deemed paid with respect to a NCTI inclusion would be limited to 90 percent of the taxes attributable to such inclusion.

These changes are proposed to apply to taxable years of foreign corporations beginning after December 31, 2025, and to taxable years of US shareholders in which or with which such taxable years of foreign corporations end.

For foreign tax credit limitation purposes, the tax proposal would limit the deductions that are allocated and apportioned to a taxpayer's NCTI inclusion to (1) the section 250 deduction attributable to a NCTI inclusion (including any foreign income taxes attributable to such NCTI inclusion), and (2) any other deductions only to the extent they are directly allocable to a NCTI inclusion. Any deductions that would have been allocated and apportioned to a NTCI inclusion are instead allocated and apportioned to US-source income (*i.e.*, they do not reduce the foreign tax credit limitation in other categories). These changes are proposed to apply to taxable years beginning after December 31, 2025.

Modification of source rules for foreign offices or fixed places of business: The Finance Committee proposal would modify the sourcing rules for taxable income from sales of inventory manufactured by the taxpayer in the US and sold through an office or fixed place of business in a foreign country. Up to 50 percent of such income would be treated as foreign-source income for purposes of the foreign tax credit limitation. This change is proposed to apply to taxable years beginning after December 31, 2025.

Modification of the Foreign-Derived Intangible Income ("FDII") deduction: The Finance Committee proposal would modify the FDII regime to remove the impact of a corporation's QBAI, and generally allows a deduction of 33.34 percent of the corporation's entire foreign-derived deduction eligible income ("FDDEI") (rather than FDII). This will generally result in an effective tax rate related to FDDEI of 14 percent.

It would also exclude certain types of income from being treated as deduction eligible income ("DEI") or FDDEI. DEI (and FDDEI) would not include (1) income or gain from the sale or disposition of property that gives rise to rent or royalties and (2) certain passive income. These proposals would apply to sales or other dispositions occurring after June 16, 2025, and to income received or accrued after such date.

It would limit the deductions allocable and apportionable to DEI (and FDDEI) to only those deductions that are directly related to such income.

Unless otherwise noted above, these changes are proposed to apply to taxable years beginning after December 31, 2025.

Modification of the Base Erosion and Anti-Abuse Tax ("BEAT"): The Finance Committee proposal would modify the definition of an "applicable taxpayer" by reducing the base erosion percentage threshold, for all taxpayers, to 2 percent. The current general threshold is 3 percent. The other conditions for applicable taxpayer status (*i.e.*, the gross receipts threshold and type of corporation) remain unchanged.

It would increase the BEAT rate to 14 percent for all taxpayers (*i.e.*, BEAT would equal the excess of 14 percent of modified taxable income over adjusted regular tax liability). Additionally, it would repeal the scheduled 2026 changes in the treatment of certain tax credits.

Certain payments to related parties that are subject to a sufficient rate of foreign tax would be excluded from the definition of a base erosion payment ("BEP"). This includes payments subject to an effective rate of foreign income tax that is greater than 90 percent of the highest rate of tax under section 11 (generally, 18.9 percent), subject to an exception for certain related party payments that may fund payments to other foreign persons that are not subject to a sufficient rate of foreign tax.

The Finance Committee proposal would also expand the definition of a BEP to include certain amounts of capitalized interest paid to foreign related parties (other than interest that is charged to a capital account under section 263(g) or section 263A(f)). It would make conforming amendments to the definition of a base erosion tax benefit and the base erosion percentage for a taxpayer consistent with the above.

These changes are proposed to apply to taxable years beginning after December 31, 2025.

Permanent extension of look-thru rule for Controlled Foreign Corporations ("CFCs"): The Finance Committee proposal would permanently extend the CFC look-thru rule of section 954(c)(6).

Repeal of election for 1-month deferral in determination of taxable year of specified foreign corporations: The Finance Committee proposal would eliminate the option for specified foreign corporations to use a one-month deferral taxable year. Consequently, a corporation that previously used a one-month deferral year must align its taxable year with that of its majority US shareholder. This change is effective for taxable years of specified foreign corporations beginning after November 30, 2025, subject to a transition rule.

Restoration of limitation on downward attribution of stock ownership in applying constructive ownership rules: The Finance Committee proposal would reinstate section 958(b)(4), the restriction on downward attribution of stock ownership when applying the constructive ownership rules for section 958(b) purposes.

Additionally, it would add proposed section 951B, which permits downward attribution from a foreign person in specific situations. Pursuant to proposed section 951B, a foreign-controlled US shareholder ("FCUSS") of a foreign-controlled foreign corporation ("FCFC") is subject to CFC inclusion rules (*e.g.*, subpart F, NCTI inclusions (currently known as GILTI)) as though the FCUSS were a US shareholder and the FCFC were a CFC.

An FCUSS is a US person who would be considered a US shareholder of a foreign corporation if such person owned more than 50 percent of the stock of such foreign corporation and downward attribution from foreign persons applies. A FCFC is a foreign corporation (other than a CFC) that is more than 50 percent owned by at least one FCUSS. Sections 958(a) and 958(b) (but excluding section 958(b)(4)) apply for purposes of determining whether this ownership threshold is met.

Regulatory authority is provided for treating a FCUSS or a FCFC as a US shareholder or as a CFC, respectively, for purposes of other provisions.

These changes are proposed to apply to taxable years of foreign corporations beginning after December 31, 2025, and to taxable years of US shareholders in which or with which such taxable years of foreign corporations end.

Modifications to pro rata share rules: The Finance Committee proposal would amend section 951 and section 951A to require that every US shareholder of a CFC who owns stock in the corporation during its tax ("CFC year") to include their pro rata share of the CFC's subpart F income in gross income for the CFC year. US shareholders who own stock on the last day of the CFC year when the corporation is a CFC must also include the section 956 amount for that year.

The pro rata share of subpart F income is based on the amount of income attributable to the stock owned by the US shareholder and the period during which they were a US shareholder while the corporation was a CFC. Comparable rules apply when for purposes of determining a US shareholder's NCTI inclusion.

These changes are proposed to apply to taxable years of foreign corporations beginning after December 31, 2025, and to taxable years of US shareholders in which or with which such taxable years of foreign corporations end.

Section 899 enforcement of remedies against unfair foreign taxes: The Finance Committee proposal, like the House-passed bill, would add a new section 899. The Finance Committee's version of section 899 would increase tax rates on certain foreign persons in jurisdictions that impose an "extraterritorial tax," defined to include the Undertaxed Profits Rule (UTPR). The legislative language would impact investors from foreign countries that have enacted such taxes. It would also be expected to both increase the number of corporations subject to the BEAT and increase the amount due under BEAT for certain corporations that are organized in a jurisdiction with an "unfair foreign tax," or that are controlled by one or more persons tax resident in such a jurisdiction (an "offending foreign country").

For purposes of proposed section 899, an unfair foreign tax generally includes an extraterritorial tax or a discriminatory tax, the latter of which includes a digital services tax (DST). In a departure from the House approach, this proposal would not begin to apply to calendar year taxpayers prior to January 1, 2027. Further differences between this committee proposal and the House-passed bill with respect to section 899 are discussed below.

Proposed section 899 would apply to "applicable persons," which includes (i) governments of foreign countries, (ii) certain individual tax residents of offending foreign countries (excluding US citizens or residents), (iii) certain foreign corporations either tax resident in offending foreign countries or majority owned by other applicable persons, (iv) private foundations created or organized in offending foreign countries, and (v) certain trusts majority owned by applicable persons. For foreign corporations, an exemption from treatment as an applicable person can apply when the corporation is a US-owned corporation within the meaning in section 904(h)(6) or is publicly held, which is a defined term in the bill.

Proposed section 899 would generally increase rates of tax imposed on foreign persons': effectively connected income (ECI) and non-ECI FDAP income. Also increased would be the rates of the branch profits tax (for purposes of section 884) and the tax imposed by section 4948(a). The rates would be increased in up to three 5-percentage-point annual increments. The rate increases would apply on top of the rate imposed by statute, as modified by an applicable tax treaty (if any). In a change from the House-passed bill, the maximum percentage point increase in this proposal is 15 percent, measured from the statutory or treaty rate. Thus, for a foreign person subject to a "zero" treaty rate on non-ECI FDAP income, the rates could escalate to at most 15 percent in year 3 and thereafter. However, for individuals, the tax increase on ECI remains limited to such persons' Foreign Investment in Real Property Tax Act (FIRPTA) gains.

Unlike the House-passed bill, the Finance Committee proposal would provide express rules for when a tax exemption, exception or zero rate is treated as subject to the rate increases in the bill. Specifically, non-ECI FDAP of certain foreign individuals or foreign corporation, ECI of foreign corporation, and, the private foundation tax are all treated "zero rate income" (when no tax is imposed) and rate increases are tacked on when otherwise applicable. However, the branch profits tax, when prohibited by treaty – but not when permitted at a reduced rate – appears to be unaffected by the rate changes in the Finance Committee's proposal.

Like the House-passed version of section 899, this proposal would repeal the exemption provided to foreign governments in section 892 from offending foreign countries. However, certain other statutory exemptions are specifically preserved, including short term original issue discount, the portfolio interest exemption, certain dividends from regulated investment companies, and deposit interest. While there is regulatory authority to provide guidance with respect to other statutory exemptions, the addition of these specific provisions may call into question the interaction of the bill with other statutory exemptions not mentioned in the bill.

With respect to withholding taxes, the Finance Committee proposal would similarly increase rates of withholding by 5 percentage points per year under each of section 1441 (other than the 14 percent rate specified in section 1441(a)), section 1442, and section 1445.

As noted previously, the Finance Committee proposal would not apply prior to January 1, 2027. The specific date (and rate) increase varies based on the relevant offending foreign country and the foreign person's tax year.

Commentary: Considering the delayed effective date of these provisions to 2027, taxpayers that can control when they make FDAP payments may want to consider making any such payments within their control to affected foreign persons prior to the application of section 899.

As in the House-passed bill, the application of the rate increases for withholding agents appears to be limited in many cases until the Treasury Department publishes a list of counties imposing an unfair foreign tax.

However, as in the House-passed bill, this relief does not appear to apply to withholding agents under section 1446(a) (partnership ECI withholding).

New section 899 would also modify the application of BEAT to certain corporations in which more than 50 percent of the total combined voting and total value of their stock is owned (within the meaning of section 958(a)) by applicable persons (defined above). Such corporations ("applicable corporations") (1) are deemed to satisfy the gross receipts test; (2) are deemed to satisfy the base erosion percentage test when their base erosion percentage hits 0.5 percent; (3) do not benefit from the favorable treatment of section 41 credits and applicable section 38 credits, (4) cannot apply exceptions for amounts qualifying for the services costs method ("SCM") or subject to US withholding tax or satisfying the new rule in the bill for payments subject to sufficient foreign tax; and (5) must treat amounts capitalized that (a) are not the purchase price of depreciable or amortizable property or inventory, and (b) that otherwise are treated as base erosion payments (BEPs) as deductions for purposes of calculating BEPs and base erosion tax benefits (BETBs).

This proposal would also add a rule to coordinate with existing section 891.

Passthrough entities

The Finance Committee's proposal would permanently extend the passthrough business deduction – a key provision originally enacted under the TCJA.

Extension of deduction for qualified business income and permanent enhancement: Under current law, section 199A generally provides for a potential deduction to an individual, estate, or trust of up to 20 percent of the qualified business income (QBI) from certain domestic trades or businesses operated as a sole proprietorship or through a partnership, S corporation, trust, or estate subject to certain limitations, as well as a deduction of up to 20 percent of the aggregate real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income (Combined QBI). The Combined QBI deduction cannot exceed 20 percent of taxable income less net capital gain. In addition, section 199A is available to certain patrons of all cooperatives, however, special rules are provided for specified agricultural or horticultural cooperatives and their patrons.

For taxpayers above certain taxable income thresholds, the section 199A deduction may be limited based on the W-2 wages and/or the unadjusted basis immediately after acquisition of qualified property (W-2 and Basis limitation). Above those taxable income thresholds, the deduction is phased out if the business is a specified services trade or business (SSTB). Section 199A applies to taxable years beginning after December 31, 2017, and is scheduled to expire for taxable years beginning after December 31, 2025.

The Finance Committee proposal made several modifications to section 199A, which differ significantly from the five modifications made from the House-passed bill. The first modification would make permanent the up to 20 percent deduction for QBI (including the deduction for REIT dividends and qualified PTP income) and the deduction for income attributable to certain activities of specified agricultural or horticultural cooperatives. Notably, this modification is different from the up to 23 percent permanent deduction provided in the House version. The second modification would expand the taxable income phase-in range from $100,000 to $150,000 for joint returns (in the case of non-joint returns from $50,000 to $75,000). The third modification would provide a minimum deduction for active QBI. Specifically, in the case of an applicable taxpayer, as defined below, the amount of the minimum deduction is $400. An applicable taxpayer is taxpayer who materially participates under section 469(h) and has aggregate QBI with respect to all active trades or businesses for the taxable year of at least $1000. This last modification is indexed for inflation. Notably, the House modification to include qualified BDC interest dividends in the Combined QBI amount was not included in the Finance Committee proposal.

The modifications to section 199A, as discussed above, would apply to taxable years beginning after December 31, 2025.

Exclusion of interest on loans secured by rural or agricultural real property

The Finance Committee proposal is substantially the same as the House-passed bill, except that the House-passed bill would apply only to loans made prior to January 1, 2029, and the Finance Committee proposal would make the provision permanent.

Under current law, interest income is included in gross income, however, the House-passed bill would exclude 25 percent of the interest received by a qualified lender on a qualified real estate loan from gross income. For this purpose, a qualified lender means (1) a bank or savings association the deposits of which are insured under the Federal Deposit Insurance Act, (2) any state or federally regulated insurance company, (3) any entity wholly-owned by a banking company under section 8 of the International Banking Act of 1978 that is organized and has its principal place of business in the United States, (4) any entity wholly-owned by a state insurance holding company that is organized and has its principal place of business in the United States, or (5) any federally chartered instrumentality of the United States established under section 8.1(a) of the Farm Credit Act of 1971.

A qualified real estate loan is any loan secured by rural or agricultural real estate or a leasehold mortgage on rural or agricultural real estate. The loan must be made to a person other than a specified foreign entity (as defined in section 7701(a)(51)) after the date that this provision is enacted, but prior to January 1, 2029. The exclusion from income would not apply to interest from a loan to the extent proceeds are used to refinance loans that existed prior to the enactment of this provision.

A qualified real estate loan is treated as a tax-exempt obligation for purposes of disallowing interest deductions on indebtedness incurred by qualified lenders to purchase or carry such loan.

These amendments apply to taxable years ending after the date of enactment.

Ordinary income tax rates for individuals

The TCJA made temporary changes to the ordinary income tax rates for individuals, estates and trusts, including a decrease in the top tax bracket from 39.6 percent to 37 percent. The House-passed bill would make those changes permanent. The Senate legislative language would do the same. Thus, the top ordinary income tax bracket would continue to be 37 percent.

Under current law, the ordinary income tax brackets are subject to a cost-of-living adjustment to account for inflation. The House-passed bill would generally modify the indexing for inflation for bracket thresholds by providing one additional year of inflation in the cost-of-living adjustment. However, under the bill, the dollar amount at which the 37-percent rate bracket begins and the 35-percent rate bracket ends would not be provided this additional year of inflation in the cost-of-living adjustment. The Finance Committee proposal would instead provide an additional year of inflation adjustment to the 10 percent, 12 percent and 22 percent rate brackets.

Individual deductions, personal exemptions, and other items to note

Standard Deductions: The House-passed bill would repeal the expiration of (and thus permanently extend) the temporary increases to the standard deduction amounts that were enacted under the TCJA. In addition, the House-passed bill would temporarily increase the amount of the standard deduction by $2,000 in the case of married individuals filing a joint return and a surviving spouse, $1,500 in the case of a head of household, and $1,000 in any other case for taxable years beginning after December 31, 2024, and before January 1, 2029. These temporary amounts are not indexed for inflation. Additionally, the House-passed bill would provide for a temporary bonus standard deduction of $4,000 for senior citizens who have reached age 65 for taxable years beginning after December 31, 2024, and before January 1, 2029 ("the senior bonus amount"). The senior bonus amount is phased out for taxpayers with modified adjusted gross income (MAGI) that exceeds $150,000 for taxpayers filing jointly or $75,000 for all other taxpayers. The senior bonus amount is phased out by 4 percent of the amount that exceeds the indicated modified adjusted gross income (MAGI) thresholds.

The Finance Committee proposal would also repeal the expiration of the temporary increases to the standard deduction that were enacted under the TCJA. Additionally, it would permanently increase the standard deduction to $16,000 for a single filer, $24,000 in the case of a head of household and $32,000 for married individuals filing a joint return for taxable years beginning after 2025 and adjusted for inflation thereafter.

Home mortgage interest: The House-passed bill would make permanent two temporary restrictions on the deduction for home mortgage interest which were enacted under the TCJA. Specifically, under the House-passed bill, the $750,000 ($375,000 in the case of a married individual filing separately) limitation on acquisition indebtedness would be made permanent, as would the exclusion of interest on home equity indebtedness from the definition of qualified residence interest. The House-passed bill would retain the existing $1 million limitation for acquisition indebtedness incurred before December 15, 2017, including the refinancing of such indebtedness provided that the refinanced indebtedness does not exceed the principal amount of the refinanced debt.

The Finance Committee proposal would make the changes described above, and it would also treat certain mortgage insurance premiums as qualified residence interest.

Enhancement of the dependent care assistance program: The Finance Committee proposal would increase the exclusion for dependent care assistance up to $7,500 annually ($3,750 in the case of a married individual filing separately), effective for taxable years beginning after December 31, 2025. There is no identical program in the House-passed bill.

Personal casualty losses: The House-passed bill would also make permanent a temporary restriction enacted under the TCJA with respect to itemized deductions for personal casualty losses (*i.e.*, losses of property not connected with a trade or business or a transaction entered into for profit, if such losses arise from fire, storm, shipwreck, or other casualty, or from theft). Based upon this restriction, any personal casualty loss would continue to be deductible only to the extent it is attributable to a Federally declared disaster.

The Finance Committee proposal would extend deductible personal casualty losses beyond Federally Declared Disasters to also include "State Declared Disasters" effective for taxable years beginning after December 31, 2025. "State declared disasters" are defined in part as any natural catastrophe, or any fire, flood, or explosion, which is determined by the Governor of such State and the Secretary as causing sufficient damage to warrant application of the personal casualty loss rules.

Miscellaneous itemized deductions: Under the TCJA, miscellaneous itemized deductions (*e.g.*, investment expenses, certain legal fees, and unreimbursed employee business expenses) were temporarily repealed. The House-passed bill would make the repeal permanent.

The Finance Committee proposal would also make this change. In addition, it would remove unreimbursed employee expenses for eligible educators from the list of miscellaneous itemized deductions.

Itemized deduction limitation: Prior to the TCJA, the amount of certain otherwise allowable itemized deductions of a high-income taxpayer, including charitable contributions, was subject to an itemized deduction phase-out (*i.e.*, the so-called "Pease limitation"). The TCJA temporarily repealed the Pease limitation, and the House bill would make that repeal permanent. However, the House bill would introduce new limitations on itemized deductions. This provision would have the practical effect of subjecting state and local tax deductions to a greater limitation than other allowable itemized deductions for taxpayers in (or approaching) the highest tax bracket.

The Finance Committee proposal would also include a limitation on itemized deductions, but it does not include the greater limitation on state and local tax deductions. Instead, it subjects state and local tax deductions to the same limitation as other allowable itemized deductions. The Finance Committee noted that this provision would cap the value of each dollar of otherwise allowable itemized deductions at $0.35, in most cases, and applies only to taxpayers in the highest individual income tax bracket. Additionally, the itemized limitation under the Senate bill would not apply when determining the amount of the qualified business income deduction under section 199A.

0.5 percent floor on deduction of contributions made by individuals who elect to itemize: The Finance Committee proposal would impose a reduction in charitable contributions for individuals who itemize deductions. The reduction is equal to 0.5 percent of the individual's contribution base. For example, an individual with a contribution base of $1,000,000 who makes a charitable contribution of $100,000 would be able to deduct $95,000. Additionally, the provision permanently would extend the 60 percent limitation for cash gifts made to qualified charities.

Reinstatement of partial deduction for charitable contributions of individuals who do not elect to itemize: Under current law, only taxpayers who itemize are able to deduct their charitable contributions. The House-passed bill would include an above-the-line deduction of up to $150 ($300 for married filed jointly) for cash contributions to public charities (not including supporting organizations or donor advised funds) made during tax years 2025-2028 for individual taxpayers who do not itemize deductions. Charitable contribution carryovers from prior years do not qualify for this deduction. The Finance Committee proposal would increase these limits to $1,000 ($2,000 for joint filers) and make this deduction permanent.

Personal exemptions: The House-passed bill would permanently extend the TCJA's temporary repeal of the deduction for personal exemptions.

The Finance Committee proposal would permanently extend the TCJA's temporary repeal of the deduction for personal exemptions other than a newly created temporary senior deduction. For tax years beginning after December 31, 2024, and ending before January 1, 2029, a $6,000 deduction is available for each qualified individual with respect to the taxpayer. A qualified individual means, the taxpayer, if the taxpayer has attained age 65 before the close of the taxable year and, in the case of a joint return, the taxpayer's spouse if such spouse has attained age 65 before the close of the taxable year. The senior deduction shall be phased out (but not below zero) by 6 percent of so much of the taxpayer's modified gross income as exceeds $75,000 ($150,000 in the case of a joint return). The social security number of the qualified individuals are required to be included on the tax return for the tax year to qualify for the deduction.

State and local tax deduction: The cap on the SALT deduction has been a point of ongoing debate among Republican Senators. Regarding the SALT cap and Passthrough Entity Tax (PTET), the Finance Committee proposal would adopt much of the statutory framework in the House-passed bill, but diverges on several key points:

- The Finance Committee proposal would effectively create two SALT caps, one for taxes imposed at the individual level and one for "passthrough entity taxes," a new defined term. As drafted the bill would keep the individual cap at $10,000 permanently, although the Finance Committee stated that "the amount of the individual SALT cap is the subject of continuing negotiations."
- The Finance Committee proposal does not adopt the House-passed bill's distinction between "qualified trades or businesses" and "specified services trades or businesses." In addition, the Finance Committee's cap for passthrough entity taxes would apply with respect to taxes paid by pass-through entities engaged in investment activities as well as all those conducting a trade or business.

- The cap on passthrough entity taxes would generally be the greater of $40,000 or 50 percent of the individual's share of pass-through entity taxes. As such, the Senate proposal would allow for the continuation of PTET regimes, but at a reduced rate for partners and shareholders whose pass-through entity taxes exceed $40,000 (subjecting taxes above $40,000 to a 50 percent haircut).

"Passthrough entity tax" would be defined in amended section 702(d)(1)(A) as follows: "The term 'passthrough entity tax' means any tax which is described in section 164(a)(3) [a state or local income tax] … to the extent that such tax is paid or accrued in carrying on a trade or business (other than the performance of services as an employee) or an activity described in section 212." Similar rules would apply in the case of an S corporation and its shareholders.

Points in common with the House-passed bill.

Like the House-passed bill, the Finance Committee proposal would make no attempt to distinguish between entity-level business taxes (such as the NYC UBT) and PTET workaround taxes. As a result, the Finance Committee proposal would effectively eliminate 50 percent of an individual's current deduction for entity-level business taxes (to the extent the individual's pass-through entity taxes exceed $40,000).

- Also like the House-passed bill, the Finance Committee proposal would deny sole proprietorships the benefit accorded to "pass-through entity taxes."
- In addition, the Finance Committee proposal would retain both the "substitute payment" provision and the "state and local allocation mismatch provision" of the House-passed bill, with some modifications.
- As under both current law and the House-passed bill, the cap amounts ($10,000 and $40,000) would apply to all individual filers except married filing separately, whose cap amounts would be 50 percent of the standard amounts. All individuals, including married filing separately, would be subject to the same 50 percent haircut for pass-through entity taxes in excess of $40,000.

All SALT cap and PTET provisions in the Senate bill would apply to taxable years beginning after December 31, 2025. (More information about PTET is included in the State tax consideration section below.)

Alternative minimum tax: The TCJA enacted temporary increases to the alternative minimum tax (AMT) exemption amounts for individuals, as well as temporary increases to the income thresholds at which those exemption amounts are phased out. The House bill would repeal the expiration of (and thus permanently extend) those increased AMT exemptions and phase-out thresholds. The House bill would base inflation adjustments of the exemption amounts and phase-out thresholds from 2025 rather than 2017. However, the House-passed bill would apparently cause the 2026 AMT exemption and phase-out threshold amounts to be equal to the original 2018 TCJA amounts, with no inflation adjustments for the intervening years.

The Finance Committee's tax proposal would also permanently extend the increased AMT exemptions and phase-out thresholds. Under the proposal, AMT exemptions would apparently be inflation indexed from 2017, thus taking into account the inflation adjustments since the original 2018 TCJA amounts. However, the exemption phaseout thresholds under the Finance Committee proposal would in 2026 apparently revert to

2018 levels of $500,000 ($1,000,000 in the case of a joint return), with those phaseout thresholds being indexed for inflation beginning in 2027.

Deduction for tip income: A new deduction would be introduced for individuals (even those who do not itemize deductions) during tax years 2025 through 2028 who receive qualified tips in an occupation which traditionally and customarily received tips. A “qualified tip” is an amount that is paid voluntarily without any consequence in the event of nonpayment, is not the subject of negotiation, and is determined by the payor. Qualified tips do not include amounts received by the individual in the course of a specified service trade or business (as defined in section 199A(d)(2)) and exclude individuals who receive earned income in excess of the dollar amount in effect under section 414(q)(1)(B)(i), which would apparently permit an employee who is a 5 percent owner to qualify for the above-the-line deduction provided that the employee did not receive earned income in excess of the threshold. A work-eligible Social Security number is required in order to claim the deduction. Certain payors must include qualified tips in statements furnished to the Secretary.

Additionally, this provision would expand the FICA tip tax credit for a portion of the employer-paid Social Security taxes for employee cash tips to include beauty service establishments. The credit applies to tips received in connection with providing beauty services to a customer or client if tipping employees who provide the service is customary. Beauty services include barbering and hair care, nail care, esthetics, and body and spa treatments. A list of “occupations traditionally receiving tips” would be published within 90 days of enactment, if this section is enacted in its current form.

The Finance Committee proposal would limit the deduction to $25,000, reduced (but not below zero) by $100 for each $1,000 by which the taxpayer’s “modified adjusted gross income” exceeds $150,000 ($300,000 in the case of a joint return). For this purpose, modified adjusted gross income means the adjusted gross income of the taxpayer for the taxable year increased by any amount excluded from gross income under section 911, 931, 933 (for US citizens or residents living abroad or bona fide residents of certain US possessions). Additionally, the Finance Committee proposal would remove the exclusion from the definition of qualified tips amounts received in excess of the dollar amount in effect under section 414(q)(1)(B)(i) and omits the extension of tip credit to beauty service businesses. The Senate version would include a transition rule for years beginning prior to January 1, 2026, for returns or statements required to report tip amounts.

New reporting information for tipped income: The Finance Committee proposal would modify sections 6041, 6041A, and 6050W to require a payor making payment of compensation for services reportable on either Forms 1099-K, 1099-MISC, or 1099-NEC to report both the amounts of the compensation (if amounts exceed the reporting thresholds) but also to (1) separately report the portion of the payments that constitute tips and (2) indicate whether such tips are earned in an occupation described in the new section 224(d)(1) added by the OBBBA. The Finance Committee proposal is the same as the House-passed bill.

Deduction for certain overtime pay: This provision would introduce a new deduction (even those who do not itemize deductions) for individuals who receive “qualified overtime compensation” during tax years 2025 through 2028. The provision would exclude qualified tips (as defined in proposed section 224(c)) and amounts received as a highly compensated employee (as defined in section 414(q)(1)). “Qualified overtime compensation" is overtime compensation paid to an individual under Section 7 of the Fair Labor Standards Act of 1938 that is in excess of the regular rate at which such individual is employed. A work-eligible Social Security number is required in order to claim the deduction. Payors must include the total amount of qualified overtime compensation on Form W-2.

The Finance Committee proposal would limit this deduction to $12,500 ($25,000 for taxpayers who are married filing jointly), reduced (but not below zero) by $100 for each $1,000 by which the taxpayer's "modified adjusted gross income" exceeds $150,000 ($300,000 MFJ). For this purpose, modified adjusted gross income means the adjusted gross income of the taxpayer for the taxable year increased by any amount excluded from gross income under section 911, 931, 933 (for US citizens or residents living abroad or bona fide residents of certain US possessions). Additionally, the Finance Committee proposal would remove the exclusion from qualified overtime compensation amounts received as a highly compensated employee under section 414. The Finance Committee proposal would require a statement to be furnished for the secretary and to the payee reporting qualified overtime compensation paid to persons not treated as employees under tax laws and includes a transition rule for years beginning prior to January 1, 2026, for returns or statements required to report overtime amounts.

The Finance Committee proposal would modify section 6041 to require a payor making payment of compensation for services reportable on Form 1099-MISC/-NEC to report the amount of the compensation (if amounts exceed the reporting thresholds) but also to separately report the portion of the payments that constitute an amount of qualified overtime compensation.

Deductibility of car loan interest: This provision creates an above-the-line deduction of up to $10,000 for qualified passenger vehicle loan interest during a given taxable year. This deduction is available for interest paid from tax year 2025 through 2028. This deduction begins to be phased out when the taxpayer's modified adjusted gross income exceeds $100,000 ($200,000 in the case of a joint return). This provision is expansive and includes numerous types of personal and recreational vehicles within the definition of a qualified passenger vehicle. In addition to specific language dictating which vehicles are considered a qualified passenger vehicle, the provision also establishes that this deduction is only available for vehicles of which final assembly occurs in the United States.

The Finance Committee proposal would make this interest deductible after the calculation of adjusted gross income, but the deduction would nevertheless reduce taxable income even for those taxpayers who do not itemize deductions (akin to the section 199A deduction). Unlike the House-passed bill, the Finance Committee proposal would require that the original use of the applicable passenger vehicle commence with the taxpayer. In defining an "applicable passenger vehicle," the Senate bill would replace specific references in the House-passed bill to all-terrain vehicles, trailers and campers with requirements that the vehicle have a both gross vehicle weight rating of less than 14,000 pounds and be treated as a motor vehicle for purposes of title II of the Clean Air Act. The Finance Committee proposal would also require as a condition of deductibility that the taxpayer's tax return include the vehicle identification number of the applicable passenger vehicle.

Wagering losses: Losses sustained during a taxable year on wagering transactions are allowed as a deduction only to the extent of the gains during the taxable year from such transactions. The TCJA enacted a temporary provision, described in the legislative history as a “clarification,” that the scope of the term “losses from wagering transactions” includes any deduction allowable under chapter 1 of the Internal Revenue Code. Thus, the limitation on losses from wagering transactions applies not only to the actual costs of wagers but also to other expenses incurred in connection with gambling activity (such as the otherwise deductible costs of travel to and from a casino). The House-passed bill would make this provision permanent.

The Finance Committee proposal would also make permanent the TCJA provision regarding the scope of losses from wagering transactions. In addition, it would limit wagering losses allowed to 90 percent of such losses incurred during the taxable year, and such losses would only be allowed to the extent of gains from such transactions during such taxable year.

Moving expenses: The TCJA temporarily repealed the above-the-line deduction for moving expenses paid or incurred in connection with the commencement of work at a new principal place of work. The temporary repeal does not apply to certain members of the Armed Forces on active duty. Similarly, the TCJA temporarily repealed the exclusion from gross income and wages for qualified moving expense reimbursements received from an employer, except in the case of certain members of the Armed Forces on active duty. The House-passed bill would permanently repeal the deduction for moving expenses and the corresponding exclusion from gross income for reimbursements from an employer. As under current law, the repeal of these provisions would not apply to certain members of the Armed Forces.

The Finance Committee proposal would make these same changes, but it would also allow the deduction of moving expenses and the corresponding exclusion from gross income for certain members of the Intelligence Community.

Business-related meals: Section 274(n)(1) currently limits the amount of meal expenses allowed as a deduction to 50 percent of the amount of such expenses paid or incurred. Any amounts incurred and paid after December 31, 2025, are not deductible (section 274(o)). Under current law, expenses for food or beverages required by Federal law to be provided to crew members of a commercial vessels are excepted from the limitation under section 274(n)(1) and restriction under section 274(o). The Finance Committee proposal proposed to maintain the current laws and exceptions and would add meals provided on certain fishing boats and at certain fish processing facilities as another exception. The amendments would apply to amounts paid or incurred after December 31, 2025.

Discharge of student loans: The TCJA included a temporary provision which provided an exclusion from gross income for an otherwise includible amount from the discharge of certain education loans on account of a student’s death or total and permanent disability. The American Rescue Plan Act of 2021 (P.L. 117-2) temporarily expanded this exclusion to make it applicable irrespective of whether the discharge is because of a student’s death or total and permanent disability. The House-passed bill would make permanent the temporary exclusion under the TCJA for an otherwise includible amount from the discharge of a qualifying loan on account of a student’s death or total and permanent disability. The House-passed bill’s exclusion from gross

income is permitted in respect of a discharge during a taxable year only if the taxpayer includes on the tax return for the year the taxpayer's social security number and, if the taxpayer is married, the social security number of the taxpayer's spouse.
URL: https://www.congress.gov/117/plaws/publ2/PLAW-117publ2.pdf

The Finance Committee proposal does not contain language regarding joint returns for married persons and inclusion of the social security number of the taxpayer's spouse on the tax return. Otherwise, this provision of the Senate bill is consistent with the House bill.

Bicycle commuting reimbursement: Prior to the TCJA, qualified bicycle commuting reimbursements of up to $20 per qualifying bicycle commuting month in a calendar year were excludible from an employee's gross income. The TCJA temporarily repealed that exclusion from gross income. The House-passed bill would make that repeal permanent.

The Finance Committee proposal would also permanently repeal the qualified bicycle commuting reimbursement exclusion. However, for qualified transportation fringe benefits, other than the qualified bicycle commuting reimbursement, the Senate bill adds an additional year of inflation adjustment.

Hazardous duty area for members of the armed forces: The TCJA provides that a qualified hazardous duty area is temporarily treated in the same manner as a combat zone for purposes of determining eligibility for certain tax benefits available to members of the Armed Forces. The House-passed bill would make that provision permanent. In addition, the House-passed bill would modify the definition of a qualified hazardous duty area to include the Sinai Peninsula of Egypt, Kenya, Mali, Burkina Faso, and Chad, in certain circumstances.

The Finance Committee proposal does not make any material changes to this section.

Achieving a Better Life Experience (ABLE) account enhancements: Pre-TCJA law created tax-preferred savings accounts for payments of qualified disability expenses of a designated beneficiary, with contributions subject to various limitations. The TCJA temporarily enhanced the account provisions to make contributions eligible for the nonrefundable "savers credit," permit nontaxable rollovers from qualified tuition programs, and permit account beneficiaries who work and earn income to contribute above the ABLE contribution limit. The House-passed bill makes the enhancements to the ABLE account provisions permanent.

The Finance Committee proposal does not make any material changes to these sections.

Limitations on Eligibility for Advance Payments of Health Insurance Premium Assistance Payments: Under current law, certain individuals may receive advance payments of premium assistance credits in order to purchase health insurance through an American Health Benefit Exchange. The House-passed bill would restrict eligibility for the premium assistance credit to individuals who are lawfully admitted to the US for permanent residence, certain citizens of Cuba, and individuals living in the US through a Compact of Free Association. The

House-passed bill would also limit eligibility for certain cost-sharing reductions and eligibility for a basic health program to similar categories of individuals.

The Finance Committee proposal would make no substantive changes relative to the House-passed bill.

Additional restrictions on health insurance premium tax credits: Under current law, individuals who are "lawfully present" in the US are allowed to received premium tax credits to purchase health insurance through an American Health Benefit Exchange. The House-passed bill would restrict individuals with immigration status granted by asylum, parole, temporary protected status, deferred action or deferred enforced departure, and withholding of removal from receiving premium tax credits. In addition, the proposal would cause individuals who are lawfully present aliens and ineligible for Medicaid by reason of alien status to be ineligible for premium tax credits.

Current law also provides that excess advance payments of the premium assistance credit are treated as an additional tax liability on the individual's income tax return (*i.e.*, recaptured), subject to a limit on the amount of additional liability in certain cases. The House-passed bill would provide that, for an individual with household income below 400 percent of federal poverty level, the recapture of the excess advance payments is no longer limited.

Finally, the House-passed bill would provide that the premium assistance credit is unavailable with respect to a specific plan through which an individual has enrolled using the monthly special enrollment period available for individuals with projected annual household income no greater than 150 percent of the federal poverty level.

The Finance Committee proposal would make no substantive changes relative to the House-passed bill.

School expenses for 529 accounts: Cash distributions from a qualified tuition program (also known as a section 529 plan) that are attributable to earnings on contributions to the account are included in the account beneficiary's income only to the extent that total cash distributions during the taxable year exceed the amount of qualified higher education expenses of the account beneficiary during that year. The amount of cash distributions from all qualified tuition programs related to elementary or secondary schools are limited to $10,000 per beneficiary per taxable year. The House-passed bill would expand the definition of qualified higher education expenses related to elementary or secondary schools to include not only tuition, but also curriculum and curricular materials, books or instructional materials, certain tutoring expenses, standardized achievement test fees, and certain educational therapies for students with disabilities.

The Finance Committee proposal would remove qualified expenses incurred in connection with a homeschool, which were explicitly included in the House-passed bill, from the definition of the term "qualified higher education expense."

Credentialing expenses / 529 accounts: The House-passed bill would add a new category of "postsecondary credentialing expenses" to the definition of "qualified higher education expenses" under section 529.

"Qualified postsecondary credentialing expenses" include a broad category of tuition and other expenses related to certain approved postsecondary programs, such as vocational training.

The Finance Committee provision would make no material changes relative to the House-passed bill.

Qualified disaster losses: Personal casualty losses meeting the definition of Qualified Disaster Losses are afforded special taxpayer favorable treatment. Most notably, taxpayers qualifying to use these special rules are not required to reduce their casualty loss deduction by 10% of their adjusted gross income. Under current law, these special rules only apply to a major disaster declared by the President before February 11, 2025, the incident period must have started before December 12, 2024, and such incident period must have ended by January 11, 2025. Under the House-passed bill, the special rules related to Qualified disaster losses would be extended as the applicable end dates would coincide with the date the bill is signed into law. If this bill becomes law, certain disasters that occurred near the end of 2024 or the beginning of 2025 would now appear to meet the definition of Qualified Disaster Losses.

The Finance Committee proposal would make no material changes to this section as compared to the House-passed bill.

Section 1202 expansion of qualified small business stock gain exclusion: Very generally, a taxpayer must hold Qualified Small Business Stock ("QSBS") for more than five years to qualify for the section 1202 exclusion from gross income. The exclusion is currently the greater of 1) $10 million, reduced by the aggregate amount of gain exempted in prior years, or 2) ten times the aggregate adjusted basis of stock issued by such corporation that was disposed in the taxable year. Under section 1202(a), a taxpayer's applicable exclusion amount depends on the date the stock is issued. For example, the applicable percentage is 100 percent for stock issued after September 27, 2010. In addition, in order for the stock to qualify as QSBS, the company must meet a number of requirements, including to be treated as a qualified small business, which includes the gross asset test.

The Finance Committee proposal would make a number of modifications to section 1202. First, it would modify the applicable exclusion percentage creating a tiered gain exclusion amount, depending on the date the stock was issued. Additionally, regardless of the applicable exclusion percentage, an AMT adjustment would not apply to stock acquired subject to these modifications. Specifically, the tiered gain exclusion amounts are the following:

- The applicable percentage for stock held for more than 3 years but less than four years is 50 percent.
- The applicable percentage for stock held for more than 4 years but less than 5years is 75 percent .
- The applicable percentage for stock held for more than 5 years is 100 percent.

In addition, the Finance Committee proposal would increase the eligible gain exclusion amount from $10m to $15m. Furthermore, the $15 million exclusion amount would be adjusted for inflation beginning in 2027. However, the increases would not apply to taxpayers who fully utilized the exclusion amount in a prior year.

It would also increase the gross asset threshold from $50 million to $75 million, which would be adjusted for inflation.

Generally, the effective date for the above changes is the enactment date of this Act and such changes appear to be permanent. For example, the graduated exclusion percentages and increase to the eligible gain amount applies to stock acquired on or after the date this provision is enacted. For this purpose, the acquisition date is determined after the application of section 1223.

Allow for payments to certain individuals who dye fuel: There is no current provision in the Code that permits a payment to an individual that removes from a terminal dyed diesel fuel or kerosene on which a section 4081 tax was previously imposed. The Finance Committee proposal would add new section 6435 to the Code, which provides for a payment to a person who removes from a terminal eligible indelibly dyed diesel fuel or kerosene. The term “eligible indelibly dyed diesel fuel or kerosene” is defined in new section 6435 to mean diesel fuel or kerosene on which a tax under section 4081 was previously paid and not credited or refunded, and which is exempt from taxation under section 4082(a). The provision also makes conforming amendments to sections 6206, 6430, and 6675.

The changes made by the Finance Committee would apply to eligible indelibly dyed diesel fuel or kerosene removed on or after the date that is 180 days after the date of enactment of this section.

Trump accounts: This provision in the House-passed bill would create a new type of tax-preferred account, a “Trump account,” effective for account contributions made on or after January 1, 2026. Trump accounts would function similarly to section 529 plans (explained above) but are subject to different qualifications and distribution rules. An individual may generally only be named as the account beneficiary of one Trump account, except for certain rollover accounts.

A Trump account could only be created for an account beneficiary under age eight on the date such account is created. Cash contributions to a Trump account would be limited to $5,000 annually (indexed for inflation) and could only be made while the account beneficiary is under age 18. Excess contributions would be subject to a 6 percent excise tax. These accounts would be subject to certain trustee and investment requirements, and trustees of these accounts would be subject to information reporting requirements.

Trump account distributions would begin only after the account beneficiary reached age 18. Distributions of up to one-half the cash equivalent value of the account as of the date the beneficiary turned 18 could be made when the beneficiary is between ages 18 and 25. Upon attaining age 31, the account would cease to be a Trump account and would be considered distributed to the account beneficiary.

Distributions from a Trump account used for qualified expenses would be taxable as capital gains. Other distributions would be includible in income and subject to an additional tax of 10 percent if made to a beneficiary under age 30. In the case of any distribution, the portion attributable to the investment in the contract is not includible in gross income. Qualified expenses would include qualified higher education expenses, qualified post-secondary credentialing expenses, amounts paid or incurred with respect to any small business which the beneficiary has obtained through a small business loan, small farm loan, or similar loan under regulations provided by the Treasury Secretary, and amounts used for the purchase of a principal residence of an account beneficiary who is a first-time homebuyer.

The Finance Committee proposal would make no substantive changes relative to the House-passed bill.

Trump accounts contribution pilot: This section of the House-passed bill would provide for a pilot program for a government-funded one-time credit of $1,000 to the Trump account of each qualifying child of a taxpayer who is a child born after December 31, 2024, and before January 1, 2029, who is a US citizen at birth.

The Senate Bill would make no substantive changes relative to the House-passed bill.

Individual credits

Child tax credit: The TCJA temporarily increased the child tax credit from $1,000 to $2,000 per qualifying child. The House bill would permanently extend the expanded child tax credit and provide further enhancements. The House bill would temporarily increase the maximum credit amount to $2,500, for tax years beginning after December 31, 2024, and before December 31, 2028. For tax years beginning after 2028, the credit would revert to a permanent amount of $2,000, indexed for inflation. The House bill would make permanent the maximum refundable portion of the credit, $1,400 per qualifying child, indexed for inflation ($1,700 in 2025). The TCJA phase-out thresholds of $400,000 for taxpayers filing jointly and $200,000 for all other taxpayers would be made permanent under the House bill. The House bill also makes permanent the $500 non-refundable child tax credit for each dependent of the taxpayer who is not a qualifying child of the taxpayer.

The Finance Committee proposal would permanently increase the nonrefundable child tax credit to $2,200 for taxable years beginning after December 31, 2024, and permanently index that credit amount for inflation beginning after tax year 2025. In addition, it would make permanent the refundable child tax credit of $1,400, adjusted for inflation ($1,700 in 2025). It would also make permanent the increased income phase-out threshold amounts of $200,000 ($400,000 in the case of a joint return), as well as the $500 nonrefundable credit for each dependent of the taxpayer other than a qualifying child.

Enhancement of adoption credit: Existing law allows eligible taxpayers to claim a nonrefundable credit, up to an annually adjusted maximum amount and subject to AGI limitations, for qualified adoption expenses. The House-passed bill would make the adoption tax credit partially refundable up to $5,000 (indexed for inflation) beginning in tax years starting after December 31, 2024. The refundable portion of the credit cannot be carried forward.

The Finance Committee proposal would make no changes to the adoption credit relative to the House-passed bill.

Enhancement of child and dependent care tax credit: A taxpayer with one or more qualifying individuals, such as a child or other dependent, may claim a credit against income tax liability for employment-related expenses for child and dependent care. The Finance Committee proposal would increase the maximum credit rate to 50 percent (currently 35 percent), reduced by one percentage point, but not below 35 percent, for each $2,000 or fraction thereof by which the taxpayer's AGI exceeds $15,000. This provision is effective for taxable years after December 31, 2025.

Recognizing Indian tribal governments for purposes of determining whether a child has special needs for purposes of the adoption credit: Under current law, state governments can determine whether a child has "special needs" for purposes of the adoption tax credit. The House-passed bill would provide Indian tribal governments the same ability as state governments to determine whether a child has special needs for the purposes of the adoption tax credit.

The Finance Committee proposal would make no changes as relative to the House-passed bill.

Social security number requirement for American Opportunity and Lifetime Learning Credits: Under current law, a taxpayer is permitted the American Opportunity Tax Credit or Lifetime Learning Credit in a taxable year in respect of the education of an individual only if (among other requirements) the taxpayer includes on the taxpayer's tax return for that year the taxpayer identification number ("TIN") of that individual. The House-passed bill would replace the present law TIN requirement with a rule that a taxpayer is allowed the American Opportunity Tax Credit or Lifetime Learning Credit in a taxable year only if the taxpayer includes on the tax return for that year (1) the taxpayer's social security number, (2) in the case of a joint return, the taxpayer's spouse's social security number, and (3) in respect of qualified tuition and related expenses of an individual other than the taxpayer or the taxpayer's spouse (for example, a dependent child of a taxpayer parent), that individual's name and social security number.

The Finance Committee tax proposal would make no substantive changes relative to the House-passed bill.

Updates to Earned Income Tax Credit ('EITC"): The House-passed bill would require the Secretary of the Treasury to establish a program under which the Secretary is required to issue, in response to a taxpayer's application with respect to a child, an EITC certificate to establish a child's status as a qualifying child only of the taxpayer for a taxable year. It would also increase the credit amount for specified Purple Heart recipients.

The Finance Committee proposal is largely the same as the House-passed bill, except for a modification to the calculation of the credit amount for specified Purple Heart recipients who are not eligible individuals for the taxable year.

Permanent extension of the new markets tax credit: Under current law, section 45D provides a competitively awarded credit to taxpayers who make qualified equity investments in certified community development entities, which in turn use substantially all of the investment to make qualified low-income community investments in low-income communities or for the benefit of low-income persons. Low-income communities are designated by the Community Development Financial Institutions Fund (CDFI), a bureau within Treasury. The credit is claimed over a 7-year period, with 5 percent of the investment amount allowed as a credit in each of the first three years, and 6 percent in each of the following four years, totaling 39 percent of the investment.

The Finance Committee proposal would permanently extend this credit and establishes an annual pool of $5 billion of tax credit allocation investment authority each calendar year beginning after December 31, 2025.

Estate and gift tax

Under the provisions of the House bill, the existing transfer tax architecture (the estate, gift and generation-skipping transfer taxes) would be retained, with one modification: the basic exclusion amount (*i.e.*, the amount that each citizen and US domiciled person is entitled to transfer either during life or, if otherwise unused, at death without incurring a current tax) and the generation-skipping transfer tax (GST) exemption (*i.e.*, the amount that may be transferred to skip persons outright or in trust without giving rise to a present or future GST tax) would be increased to $15 million from its existing $10 million (before adjustment for inflation) for transfers occurring after December 31, 2025. The $15 million threshold would be indexed for inflation in years after 2026. Unlike the increase to the basic exclusion amount under current law, the $15 million is permanent and thus is not scheduled to revert to a lesser amount in the future.

The Finance Committee proposal does not make any material changes relative to the House-passed bill.

Filing updates

Task force on termination of Direct File: Consistent with the House-passed bill, the Finance Committee proposal would terminate the Direct File program, which currently allows the IRS to prepare and file tax returns online for free for certain qualifying taxpayers in participating states. Instead, the Department of Treasury would establish a task force that would report to Congress on the cost of a new public-private partnership to provide for free tax filing for up to 70 percent of all taxpayers. The report would also provide taxpayer opinions and preferences regarding such a partnership in addition to an assessment of the feasibility and costs needed.

Increase in penalties for unauthorized disclosures of taxpayer information: Currently, the maximum fine for an unauthorized disclosure of taxpayer information under section 6103 is $5,000, and the maximum term of imprisonment upon conviction is five years. The Senate provision, which is the same as the House-passed bill, would increase the maximum fine to $250,000, and it would also increase the maximum term of imprisonment upon conviction to 10 years. The Finance Committee proposal also would clarify that a willful unauthorized disclosure involving the returns or return information of multiple taxpayers are separate violations for each such taxpayer.

Backup withholding and reporting

TCJA extension and backup withholding: When a payor makes a payment of a kind that would be reported on a Form 1099, they are generally required to obtain the US Taxpayer Identification Number (TIN) of the payee.

If the payee does not provide their TIN, the payee is required to withhold a certain amount from the payment (backup withholding) under section 3406. The amount required to be withheld is the fourth lowest rate of tax under section 1(c). The TCJA modified this rate to 24 percent through calendar year 2025 in section 1(j). The Finance Committee proposal would extend the TCJA rates indefinitely, thereby cementing the 24 percent backup withholding rate past 2025.

Form 1099-K reporting and backup withholding thresholds: Reporting of payments on Form 1099-K is required for third-party settlement organizations (TPSOs) making payments of reportable payment transactions to participating payees (section 6050W). When originally enacted, no reporting was required by TPSOs on payments to participating payees if the payee had engaged 200 or fewer transactions and received $20,000 or less in payments in a calendar year. The American Rescue Plan Act (ARPA, P.L. 117-2) lowered this threshold: reporting is now required for payments made to participating payees in excess of $600, with no transaction threshold. The Finance Committee proposal would revert the threshold from $600 back to the original threshold of $20,000 and 200 transactions, retroactively effective prior to the ARPA amendment.
URL: https://www.congress.gov/117/plaws/publ2/PLAW-117publ2.pdf

The Finance Committee proposal would provide a corresponding backup withholding rule. When a TPSO has not received the TIN of the participating payee, it is only required to backup withhold once the amount of payments to the participating payee exceed $20,000 and 200 transactions. However, if the TPSO was required to backup withhold on the participating payee in the prior year, it would still be required to backup withhold in the current year if no TIN has been obtained. This rule is effective after December 31, 2024.

Form 1099-MISC/NEC reporting and backup withholding thresholds: Reporting of payments on Form 1099-MISC is required for payors making payment of a variety of fixed or determinable gains, profits, and income. (section 6041). Currently, no reporting is required where the aggregate of such payments in the calendar year are less than $600. The Finance Committee proposal raised this threshold to only require reporting where aggregate payments are $2,000 or more for calendar year 2026. For years after 2026, the $2,000 threshold would rise with inflation, using the cost-of-living calculation in existing section 1(f)(3) rounded to the nearest $100.

Payments of compensation to persons who are not employees (*e.g.*, independent contractors), are reported on Form 1099-NEC in the same manner as Form 1099-MISC. (section 6041A) The reporting threshold similarly is $600. The committee text modified the reporting threshold for such payments to reference the threshold in section 6041.

The Finance Committee proposal provided a corresponding backup withholding rule. A payor would only be required to backup withhold on payments that would be reportable under sections 6041 and 6041A if the amount is equal to or greater than the $2,000 (plus inflation for years after 2026) threshold in section 6041.

Excise taxes

Excise tax on remittance transfers: Section 70606 adds new section 4475 to the Code (as well as new Subchapter C under Subtitle D, Chapter 36) incorporating a new excise tax on certain remittances. The excise tax encompasses 3.5 percent of the amount of any "remittance transfer." The "sender" of the remittance is required to pay the tax, but the amount of the tax is collected by the "remittance transfer provider." The remittance transfer provider must remit such collected taxes quarterly. If the remittance transfer provider fails to remit the collected tax, the remittance transfer provider becomes personally liable for the owed tax. Remittance transfers that violate the anti-conduit rules of section 7701(l) can be recharacterized as financing transactions.

The Finance Committee proposal of section 4475 provides an exemption from the tax if a remittance transfer is drawn from funds held in an account with certain financial institutions described in the Bank Secrecy Act (specifically, 31 USC. 5312(a)(2)(A-E)&(G-H)). Such institutions include banks (both domestic and US branches of foreign banks), credit unions, and brokers and dealers, and the relevant account must be subject to the reporting requirements of the Bank Secrecy Act (subchapter II of chapter 53 of Title 31). Similarly, no tax is required if the remittance transfer is funded by a debit card (including a prepaid card) or credit card issued in the United States.

Covered remittance transfers include where the sender provides cash, a money order, a cashier's check, or any other similar instrument to the remittance transfer provider. Terms related to remittances are defined by reference to existing 15 USC. 1693o-1 and 1693o-2 (the Electronic Fund Transfer Act). Based on those definitions, a remittance transfer involves an electronic transfer of funds requested by a sender located in the US (or a US possession or territory) to a designated recipient located in a foreign country. A remittance transfer provider is any person or financial institution that provides remittance transfers for a natural person in the normal course of its business, whether or not the natural person holds an account with such person or financial institution. A sender is any natural person who requests a remittance provider to send a remittance transfer for the sender to a designated recipient. 15 USC. 1693o-1 indicates that a remittance transfer does not involve transfers below a *de minimis* threshold – regulations under that section list the threshold as $15.

The Finance Committee proposal would also add new section 36C to the Code. New section 36C would allow any individual to claim a credit for the amount collected and remitted to the Treasury on remittance transfers paid by such individual. The individual must provide their Social Security Number. At the time of the transfer, the remittance transfer provider must give the sender an opportunity to certify their intent to claim the credit. The sender must then provide their name, address, and Social Security Number to the remittance transfer provider. The title of new section 36C indicates that only persons with work-eligible Social Security Numbers would qualify for the credit.

Finally, the Finance Committee proposal would also add new section 6050BB to the Code. Section 6050BB requires a remittance transfer provider to file an information return with the Treasury. For transfers for which tax was collected and the sender has indicated a desire to claim the credit under section 36C, the return must include the name, address, and Social Security Number of the sender, the amount of tax paid by the sender, and the amount of the collected tax remitted by the provider. For all other remittance transfers, the return must indicate the aggregate amount of tax paid with respect to those transfers and the aggregate amount remitted to the Treasury by the provider. The provider is also required to provide an information return to any sender of a remittance transfer that includes the name and address of the provider, and the name, address, and Social Security Number of the sender. Various penalty provisions regarding information returns have been updated to account for the new return requirement.

The Finance Committee proposal would also provide that if any possession that has a mirror code tax system loses any amount of revenue due to the excise tax, the Treasury would make payments to reimburse the possession for the loss. For any possession without a mirror code tax system, the Treasury would estimate the aggregate benefits that would have been provided to residents of the possession as if such a system had been in effect. The Treasury would pay those benefits to the possession if the possession has a plan to distribute such amounts to its residents. Coordinating rules disallow the section 36C credit for persons who receive a credit from a possession government to compensate them for the tax or for whom the Treasury has reimbursed the relevant possession government.

The Finance Committee proposal is effective for transfers after December 31, 2025, and for taxable years after December 31, 2025.

Elimination of tax on certain devices under the National Firearms Act: The Finance Committee proposal would amend the definition of the term “firearm” under section 5845(a) to mean a machinegun or a destructive device. It would also remove silencers, short-barreled rifles, short-barreled shotguns, and certain devices from the definition of “firearm” for purposes of section 5845, resulting in the elimination of the transfer and manufacturing tax on these devices.

The proposal would also amend the definition of the term “destructive device” in section 5845(f)(2) to exclude shotgun shells, and any weapon designed to shoot shotgun shells.

Additionally, it would amend section 5811(a) to remove the $5 transfer tax on any firearm classified as any other weapon under section 5845(e). In effect, the amendments to the definition of “firearm” and “destructive device” would eliminate and modify certain excise taxes that are currently imposed on the transfer of firearms or any other weapon under section 5811 ($200 tax on the transfer of each firearm as defined in section 5845(a), $5 on the transfer of any other weapon under section 5845(e)), and on the making of firearms under section 5821 ($200 for each firearm made)).

The Finance Committee proposal would also amend section 5841, related to registration of firearms, by adding new section 5841(f), which treats certain registration or licensing requirement under State or local law with respect to a short-barreled rifle, short-barreled shotgun, or any other weapon (as defined in section 5845(e)), as meeting any such registration or licensing requirement with respect to that rifle, shotgun, or other weapon.

The changes made by the Finance Committee would apply to calendar quarters beginning more than 90 days after the date of enactment.

Employer-provided benefits

Educational assistance for student loan payments: Section 127 of the Code permits an employer to maintain an educational assistance program for the benefit of its employees. Under such a program, an employer can provide educational assistance (subject to certain qualification requirements related to the program) to its employees on a tax-free basis, up to a limit of $5,250 per year. The CARES Act added a temporary provision to section 127 (section 127(c)(2)(B))(to allow an employer to make payments on an employee's qualified educational loan, taken out by the employee for the employee's own education, on a tax-free basis. This particular provision was set to expire at the end of 2025. Senate Finance Committee text amended section 127 to make this provision permanent.

Section 127(a)(2) imposes an annual limit of $5,250 that can be provided tax free under an educational assistance program. Section 70413(b) of the Finance Committee proposal would provide for annual inflation indexation of this amount, beginning in years after 2026.

Tax-exempt organizations

One percent floor on deduction of charitable contributions made by corporations: The Finance Committee proposal is consistent with the House-passed bill that would amend section 170(b)(2)(A) to include a minimum threshold of charitable contribution for which corporations must meet to take a charitable contribution deduction. Under newly modified section 170(b)(2)(A), a corporation generally would be allowed a deduction for charitable contribution only to the extent the aggregate charitable contributions exceeds one percent of a taxpayer's taxable income, and does not exceed 10 percent of the taxable income. The House-passed bill would also amend section 170(d)(2) to provide that amounts that are disallowed as a result of the one percent floor can be carried forward only from years in which a taxpayer's charitable contributions exceed the 10 percent limit on charitable contributions.

The changes would apply to taxable years beginning after December 31, 2025.

Tax credit for contributions of individuals to scholarship granting organizations: This provision would add new section 4969 to Chapter 42 of the internal revenue code setting parameters for the distribution requirements for an organization to be treated as a scholarship granting organization for purposes of this credit.

The Finance Committee proposal is very similar to the House-passed bill, and would add new section 25F, Qualified Elementary and Secondary Education Scholarships, to the Code, as well as new section 139J, Scholarships for Qualified Elementary or Secondary Education Expenses of Eligible Students, and new section 4969, Failure to Distribute Receipts. The Finance Committee language would limit the section 25F credit to individuals who are citizens or residents of the United States within the meaning of section 7701(a)(9). Further, "qualified elementary or secondary education expenses" do not explicitly include expenses in connection with a homeschool, and elementary and secondary schools are not required to demonstrate maintenance of a policy where its admissions standards do not take into account certain information about students seeking enrollment. The Finance Committee proposal sets the volume cap for the section 25F credit at $4,000,000,000 for calendar year 2027 and each year thereafter and does not provide for annual increases to the volume cap like the House bill does. The amendments made by the Finance Committee apply to taxable years ending after December 31, 2026, and the exclusion from gross income for scholarships for qualified elementary or secondary educations expenses of eligible students under new section 139J shall apply to amounts received in taxable years ending after December 31, 2026.

Scholarships received from certain organizations: The House-passed bill would add new section 139J exempting scholarship income received by dependents for qualifying elementary and secondary education expenses. This provision would apply to scholarship income received after December 31, 2025, and before January 1, 2030. The Finance Committee proposal would make this new provision permanent.

Expanding application of tax on excess compensation within tax-exempt organizations: The Finance Committee proposal aligns with the House-passed bill, in that it would remove limitations to and expand the definition of "Covered Employee" under section 4960(c)(2). The provision would remove the application of the definition to only the 5 highest compensated employees and removes the extension to covered employees in a prior taxable year to only taxable years beginning after December 31, 2016. As a result, a covered employee includes any employee of an applicable tax-exempt organization that receives remuneration in excess of $1 million.

Modification of excise tax on investment income of certain private colleges and universities: Like the House-passed bill, the Finance Committee would propose a higher tax on the investment income of certain private colleges and universities. The Finance Committee proposal also, like the House-passed bill, would provide that "qualified religious institutions" are excepted from the definition of an "applicable educational institution." Further, the Finance Committee proposal would provide that "applicable educational institutions" are only schools that participated in US federal student aid programs in the tax year.

Instead of a flat excise tax of 1.4 percent, the Finance Committee proposal would provide for a tiered system ranging from 1.4 percent to 8 percent based on the institution's student-adjusted endowment. The House provision would amend the current 1.4 percent excise tax on net investment income framework for certain private colleges and universities under section 4968 with a tiered system ranging from 1.4 percent to 21 percent based on an institution's student-adjusted endowment. For purposes of calculating an institution's student-adjusted endowment, both the House-passed and the Finance Committee proposal would amend such calculation by excluding students who are not either US citizens or other allowable individuals. Additionally, both the House-passed bill and the Finance Committee proposal would increase a school's net investment income by the amount of student loan interest income and certain royalty income.

State tax considerations

Many state corporate income tax regimes are affected by federal tax law changes because states conform to the internal revenue code for purposes of administrative ease by either incorporating the IRC in whole or in part, or by using federal taxable income as the starting point. Generally, states that incorporate the IRC either:

(1) conform to the IRC as of a specific date ("Fixed Date Conformity"); or (2) automatically follow the version of the IRC in effect for the current tax year ("Rolling Conformity"). However, some states, like California, only selectively conform to specific IRC provisions ("Selective Conformity").

While Rolling Conformity states may later choose to decouple from any IRC provisions enacted by Congress through state legislative action, the Fixed Date Conformity states would continue to use a version of the IRC prior to the amendments in the Tax Bill unless and until they updated their conformity date. These differences can lead to different tax outcomes at the state level when compared to federal.

Specific provisions with potential state nonconformity: Similar to the House-passed bill, provisions which may create a federal/state disconnect in Fixed Date Conformity states include (but are not limited to) the following.

- GILTI/FDII: Certain states may continue to follow the lower deduction percentages prescribed in section 250 for years 2026 and later instead of the 40 percent and 33.34 percent deduction amounts for GILTI and FDII respectively (e.g., Arizona, Georgia, and Minnesota). This would depend largely on how each affected state views whether adopting the IRC "in effect" as of a certain date includes future operative provisions contained in the IRC as of that fixed date. States have historically taken differing views.
- Section 163(j): Certain states may continue to require the computation of adjusted taxable income without additions for depreciation, amortization, and depletion (e.g., Florida, North Carolina for corporate taxpayers and Massachusetts, New Jersey, and Pennsylvania for non-corporate taxpayers).
- Section 174: Certain states may continue to require amortization for domestic research expenditures during the period that they are not required to do so for federal tax purposes (e.g., North Carolina, Georgia).
- Section 168(n): Certain states may not allow the full expensing of "qualified production property" under new 168(n) (e.g., all fixed date states).

As was the case after the passage of the TCJA, it is anticipated that many Rolling Conformity states may decouple from some of these provisions, further complicating the conformity map.

Additionally, with the measure's potential to provide differing tax treatment based on whether activities are foreign or domestic, it is anticipated that certain provisions may be the subject of future US Constitutional challenges if enacted. The Supreme Court has held that states are generally precluded from treating domestic taxpayers more favorably than foreign taxpayers even if the state's treatment is based on administrative convenience/general conformity to federal tax law.

State and local taxes and PTET: In response to the SALT Cap enacted as part of the TCJA, a majority of states in the past few years have enacted PTET regimes where pass-through entities may elect to pay tax at the entity level, and owners are allowed a credit for their share of entity-level taxes paid or a deduction or exclusion for their share of income subject to the PTET on the owner's state personal income tax return. While each state's regime has its own nuances, it is anticipated that all may be affected by the new sections highlighted above that would limit the deductibility of certain state and local taxes, including "specified taxes" (defined to include “substitute payments”) and passthrough entity taxes and would impose a tax on partners that benefit from a “state and local tax allocation mismatch.”

It should be noted that certain state and local taxes paid by a passthrough entity other than under a PTET regime may also be impacted by the SALT Cap.

Financial Statement Considerations

Pursuant to US generally accepted accounting principles (US GAAP), the tax effects of new tax legislation are accounted for in the reporting period in which a tax law is enacted. In the US, the enactment date generally is defined as the day the president signs the legislation into law. Accordingly, because the Finance Committee proposal has not been enacted, it should not directly impact financial statements at this time. It may be prudent, however, for companies to start to analyze the impact the proposed bill may have on their tax accounts and disclosures, if enacted. If the proposal or a derivation thereof is enacted subsequent to the balance sheet date, but prior to the issuance of financial statements, the change in tax law would be considered a nonrecognized subsequent event. In that instance, companies would still need to determine whether they would need to disclose the change in law and provide an estimate of its effect in order to keep their financial statements from being misleading. To the extent potential tax code changes could materially affect the company or its business, SEC registrants should also consider possible disclosure requirements under Risk Factors and Management’s discussion and analysis of financial condition and results of operations.

— This report was prepared by the tax professionals in Deloitte Tax LLP’s Washington National Tax practice.