Tax legislative outlook for the 118th Congress

NOTE: This report was updated at 9:00 a.m. EST on February 7, 2023, and does not reflect developments after that time.

February 7, 2023

kpmg.com

This report provides information and observations regarding the outlook for federal tax legislation during the 118th Congress as of 9:00 a.m. on February 7, 2023. Read ***TaxNewsFlash Legislative Updates*** for developments after that date.

Foreword

Conventional wisdom in Washington holds that the current Congress, now under divided control, will yield little, if any, significant tax legislation. This perspective may ultimately prove true since, as is discussed in detail below, the Republican House and the Democratic Senate generally have very different tax agendas. Still, one durable truth on Capitol Hill is that Congress, no matter how divided, always seems to produce a tax bill. These tax bills often appear to come out of nowhere. But with hindsight, one can often see that the signs and the ingredients for that legislation were there all along, visible to those looking hard enough for them.

The objective of this report then is to identify the players, the components, and the motives that will drive the tax legislative agenda in the current Congress. While this document is long and covers the many aspects of the tax legislative process, users may find that the topical index that follows is useful in allowing the reader to jump to topics of particular interest.

Contents

Introduction

The 118th Congress convened on January 3, 2023. However, the House's ability to organize and conduct business was delayed pending the election of a speaker while the Senate recessed for three weeks shortly after convening and did not approve organizing resolutions until early February. The House is narrowly controlled by Republicans while the Senate is narrowly controlled by Democrats. With a single party no longer controlling both chambers of Congress and the White House, there is now "divided government."

From a tax perspective, enactment of significant changes in the direction of tax policy appears unlikely in this Congress given different views of most Democrats and Republicans on major tax policy issues. For example, although the Republican controlled House might seek to pass legislation to extend the temporary income tax rate reductions enacted as part of the so-called "Tax Cuts and Jobs Act" ("TCJA")[1] beyond 2025, the prospects of such legislation passing the Democratically controlled Senate and becoming law during this Congress appear slim. Likewise, the increases in income tax rates on corporations and high-income individuals proposed by the Biden Administration during the 117th Congress appear to have little chance of being enacted in the next two years.

Nonetheless, it is possible that some tax issues on which both Republicans and Democrats can agree might be included in legislation that can pass both chambers of Congress and be signed into law by the president. It is also possible that IRS funding levels may be reduced somewhat as part of legislation that is considered "must pass" (such as government funding legislation). Further, House and Senate tax-writing committees can be expected to hold hearings and conduct oversight activities with respect to various tax-related matters—with a different focus in the House than in the Senate.

Notably, the 117th Congress adjourned without addressing various expiring tax incentives and scheduled tax law changes, such as the TCJA provision requiring amortization of certain research and experimentation (R&E) costs for tax years that began after 2021. Although it is possible that some "tax extenders" might be addressed on a bipartisan and bicameral basis in the new Congress, the possible path forward may be rocky and enactment of legislation that includes tax extenders is far from certain. Further, any potential legislative action on tax extenders might be several months in the future at best.

Background on the new Congress

Divided government is a significant change from "one-party rule" in the 117th Congress. In that Congress, unified control of the House, Senate, and White House allowed Democrats to use special budget reconciliation procedures[2] to enact the legislation commonly called the "Inflation Reduction Act"[3] and the

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[1] **Pub. L. No. 115-97** [PDF 705 KB]
[2] See **discussion of budget reconciliation procedures** later in this report.
[3] **Pub. L. No. 117-169** [PDF 843 KB]

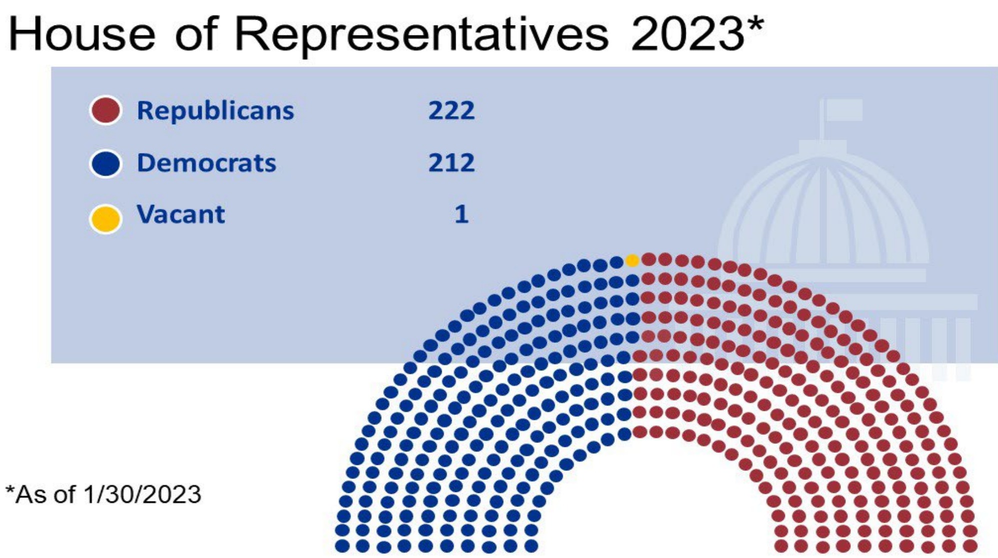
American Rescue Plan Act ("ARPA")[4] without Republican support. Similarly, in the 115th Congress (in 2017), Republicans used budget reconciliation procedures to enact the TCJA without Democratic support at a time when Republicans controlled both chambers of Congress and the White House.

By contrast, in the 118th Congress, proposed legislation would need significant support from both Republicans and Democrats to become law.

U.S. House of Representatives

In general

At the start of the 118th Congress, the House consisted of 222 Republicans and 212 Democrats, with one vacant seat due to the death of Rep. McEachin, a Democrat from Virginia, shortly after the 2022 midterm elections. A special election to fill the vacant Virginia seat has been scheduled for February 21, 2023.[5] Assuming a Democrat retains that seat, and no other vacancies arise, Republicans would control the House by nine seats—the same number of seats by which the Democrats controlled the House at the start of the 117th Congress. [6]



As explained in more detail [later in this report,] in the House, the majority party controls the legislative agenda, and it only takes a simple majority to pass most legislation.[7]

Leadership

After convening on January 3, 2023, the House spent the first several days determining who its speaker would be. As explained below, the election of the speaker took multiple ballots given the inability of virtually all House Republicans to quickly coalesce around one person. Ultimately, Kevin McCarthy (R-CA) was

[4] Pub. L. No. 117-2 [PDF 765 KB]
[5] Article I of the U.S. Constitution requires vacancies in the House to be filled by election. The governor of a state cannot simply appoint a replacement. By contrast, in the case of a vacant Senate seat, the Seventeenth Amendment to the Constitution allows state legislatures to empower the governor to make temporary appointments until the vacancy is filled by election as directed by the legislature. The decision of whether and when to hold a special election is determined by the law of each state.
[6] Note that Rep. Greg Steube (R-FL), a new member of the House Ways and Means Committee, currently is recovering from an accident he suffered in mid-January. It is not clear when he will return to Washington and be able to vote on the House floor and in the Ways and Means Committee.
[7] As indicated below, the House has adopted a rule that requires a "super majority" vote in the case of certain income tax rate increases.

elected speaker. Speaker McCarthy served as the minority leader in the 117th Congress.

Nancy Pelosi (D-CA), the speaker during the 117th Congress, stepped down as Democratic leader after the midterm elections, although she continues to represent her district in the House. The new Democratic leader is Hakeem Jeffries (D-NY).

House leadership

The vote for speaker

On November 15, 2022, shortly after the midterm elections, House Republicans voted for Kevin McCarthy to be their leader in the 118th Congress. Rep. McCarthy prevailed against Rep. Andy Biggs (R-AZ), a former chair of the conservative Freedom Caucus, by a vote of 188-31—with the number of "no" votes foreshadowing a difficult race for House Speaker at the start of the 118th Congress.

On January 3, 2023, the first order of business for the new House was to elect its speaker. Designating the Speaker requires a majority of all members voting. Typically, each party nominates and supports its own party leader to be speaker. To this end, all 212 Democratic members consistently voted for Rep. Jeffries to be speaker. However, a relatively small group of (generally) conservative Republicans voted for people other than McCarthy to be speaker in 14 rounds of voting, denying McCarthy's ability to quickly secure a majority vote.[8]

Ultimately, it took 15 rounds of votes before McCarthy won the speakership very early in the morning on January 7, 2023, with 216 Republicans voting for McCarthy, 212 Democrats voting for Jeffries, and 6 holdout Republicans voting "present." No other business could be conducted by the House prior to the determination of the speaker. Thus, for example, new House members could not be officially sworn in, committee chairs and members could not be appointed, House rules could not be adopted, and legislation could not be considered in the House.

KPMG observation

The challenges House Republicans faced in electing a speaker may presage difficulties in reaching consensus on other matters, given ideological and policy differences within the House Republican caucus.

In addition, some conservative Republican members negotiated for various concessions, including significant changes to the House rules, in exchange for supporting McCarthy in the speaker race. As explained below, some of the new rules might make it difficult for the speaker to lead the House in passing legislative measures that could also pass the Democratically controlled Senate.

New House rules

On January 9, 2023, the House approved a **rules package** that includes rules that make it easier to replace the speaker, rules that may slow down the pace of the legislative process, rules that allow "rank and file" members to play a greater role in the legislative process relative to leadership, and rules that govern

[8]Around 19 Republicans voted for a candidate other than McCarthy in the first 11 rounds of voting; however, that number dropped to seven in the 12th round and to six in the next two rounds (with those six ultimately voting "present" in the final round of voting).

consideration of certain revenue measures.[9] The new rules include the following:

- Allowing any member (Republican or Democrat) to force a vote on replacing the speaker at any time
- Requiring legislation to be posted at least 72 hours prior to a final House vote
- Eliminating proxy voting and virtual committee business[10]
- Allowing any committee chair to take a committee-approved bill of their choosing straight to the House floor on certain days
- Eliminating a rule that had provided for automatic transmittal to the Senate of a joint resolution changing the debt limit on adoption by the House of a concurrent resolution on the budget
- Allowing a point of order to be raised against any increase in an expenditure, or any new expenditure, contained in a general appropriations bill
- Permitting members to bring up amendments to general appropriations legislation that do not propose a net increase in budget authority
- Allowing amendments to spending bills to reduce the salaries of specific federal employees or to target a specific program
- Requiring a three-fifths supermajority in the House to approve any increases in individual and corporate income tax rates specified in Code section 1 (paragraphs a through e), 11(b), or 55(b)
- Replacing the "pay-go" rule that had required the costs of increases in spending or cuts in revenues in legislation to be offset by spending cuts and/or revenue raisers, with a rule that requires the cost of increased "mandatory spending" to be offset by mandatory spending cuts ("cut-go")[11]
- Requiring the Congressional Budget Office (CBO) to provide analysis on the inflationary impact of legislation
- Requiring the Joint Committee on Taxation (JCT) and the CBO to incorporate the budgetary effect of macroeconomic variables, to the extent practicable, in estimating the revenue effects of major legislation

KPMG observation

If a motion to replace the speaker were made and all Democrats supported it, it would only take the support of five Republicans to trigger a vote on a new Speaker, assuming the Virginia seat that is currently vacant has been filled by a Democrat and there have been no other changes in House membership.

[9] The vote for the rules package was 220 to 213, with 220 Republicans voting in the affirmative and one Republican and all 212 Democrats voting against the package.
[10] As indicated in n. 6 supra, one House Republican currently is recovering from an injury outside of Washington and is not yet able to return for votes.
[11] Under the House rule, the definition of "mandatory spending" is based on the definition of 'direct spending' in section 250 of the Balanced Budget and Emergency Deficit Control Act of 1985 (the "1985 Act"), but includes provisions in appropriations legislation that make certain outyear modifications to substantive law. The 1985 Act definition includes entitlement authority, the supplemental nutrition assistance program (i.e., food stamps), and law changes that result in an increase in budget authority or outlays relative to a specified budgetary baseline.

Whether one views these many rules changes as “good” or “bad” is likely in the eye of the beholder. But what is less subjective is that these changes add to the difficulty in moving legislation through the House.

In addition, Speaker McCarthy has given members of the conservative House Freedom Caucus more seats on the House Rules Committee—a powerful committee that can modify legislation before floor consideration and determine what amendments are in order. He also agreed to certain investigations and select committees that are important to some conservatives.

Further, in a **letter** [PDF 175 KB] released by McCarthy shortly before the new Congress convened, McCarthy indicated that, if he were elected speaker, committees would “once again be the primary drivers of legislation” and that he would use his selections for key panels to ensure that they more closely reflect the ideological makeup of the House Republican conference.

Possible House Republican priorities

As discussed below, once the speaker was elected, House Republicans began considering some legislative priorities and laying the groundwork for various hearings and investigations. The House is also expected to consider other legislative matters later in the year – including some matters that typically are considered to be “must pass.”

KPMG observation

Some bills that are approved by the House might signal Republican political and policy priorities, but not have sufficient bipartisan support in the Senate to move through the entire legislative process and become law. See discussion **later in this report** regarding what proposals might become law this Congress.

House Republican legislative priorities

On January 9, 2023, as its first order of legislative business, the House passed legislation (**H.R. 23**, the “Family and Small Business Taxpayer Protection Act”) to rescind approximately $71.6 billion of the additional $79.6 billion appropriated over the next 10 years for the IRS by the Inflation Reduction Act. The funds that would be rescinded include all of the additional funds appropriated in the Inflation Reduction Act for enforcement activities.[12] As reported in ***TaxNewsFlash***, the bill passed the House by a party-line vote.

KPMG observation

It would not be surprising for the House to pass similar or identical IRS “de-funding” legislation multiple times in this Congress. See **further discussion** of IRS funding later in this report

House leadership also has indicated that certain other non-tax measures would be considered on the House floor. These measures (some of which already have been addressed) include:

- Increasing oil and gas production under oil and gas leases of federal lands in conjunction with a drawdown of petroleum reserves from the Strategic Petroleum Reserve (SPR)

- Prohibiting sending petroleum products from the SRP to China

[12] The CBO has estimated that bill would increase the deficit by approximately $114 billion. Read the **CBO estimate** [PDF 147 KB]

- Authorizing the Secretary of Homeland Security to suspend the entry of aliens and other border security measures[13]
- Requiring the national instant criminal background check system to notify immigration enforcement and state and local agencies if a person unlawfully in the United States attempts to receive a firearm
- Prohibiting taxpayer funded abortions (and other abortion related matters).

Although tax issues are not expected to be among the first legislative priorities considered by the House, they were flagged as important issues in the "**Growth Through Innovation**" [PDF 419 KB] document released as part of the Republican Commitment to America in November of 2022 (before the 2022 midterm elections). That document lists a variety of tax proposals, some of which reflect significantly different policy priorities than those of many Democrats. The list below is drawn from that document and includes a very short description of proposals, along with parentheticals referencing Republican members with proposals on these issues in the 117th Congress:

- Make permanent middle-class tax cuts (Rep. Schweikert)
- Make permanent the modifications to the child tax credit made by the TCJA (Rep. Jason Smith, who has since become the Ways and Means Committee chair for the 118th Congress)
- Expand 529 savings plans to cover homeschooling and educational therapy (Rep. Jason Smith)
- Additional middle-class tax relief, plus "death tax" relief for family-owned businesses and farms
- Make permanent the tax deduction for qualified business income (Rep. Jason Smith)
- Expand startup business tax incentives (Rep. Buchanan)
- Make the interest deduction equal to a full 30% of EBITDA accounting income (Rep. Adrian Smith)
- Provide for a doubling of the R&D tax credit (the late Rep. Walorski)
- Make permanent the expensing of R&D costs (Rep. Estes)
- Provide new incentives to bring valuable intellectual property and related jobs back to the United States (Rep. LaHood)
- Permanent full expensing for investments in U.S. facilities and equipment (Rep. Arrington)
- Provide new incentives for producing American-made medicines and critical medical supplies (Rep. Wenstrup)
- Provide support for innovators developing infectious disease treatments (Rep. Buchanan)
- Provide for bonus R&D tax incentive for infectious disease research (Rep. Buchanan)[14]

Further, Speaker McCarthy reportedly may have agreed to bring to the floor a bill (**H.R. 25**, the "Fair Tax Act") to repeal the income tax, payroll taxes, and estate and gift taxes; to abolish the IRS; and to institute a

[13] Floor consideration of an immigration bill introduced by Rep. Chip Roy (R-TX) has been delayed, in part because of concerns raised by some moderate Republicans.
[14] In the 117th Congress, House Ways and Means Republicans also held a virtual meeting on making some of the temporary individual tax rates that were enacted as part of the TCJA permanent and highlighted tax law changes they would make as part of "Republicans' Commitment to An Economy That's Strong." Read a Republican Ways and Means **release** [PDF 148 KB] from the previous Congress for more information on these proposals.

national sales tax.[15] Similar legislation has been introduced in previous Congresses and is a priority for some conservative Republicans. A date for possible House consideration of this bill has not been set.

"Must pass" and other legislation

Addressing the debt limit and government funding—matters typically considered to be "must pass"—are likely to be front and center of the legislative agenda in the House (and the Senate) as critical deadlines approach. House leadership has expressed support for using "must pass" legislation to advance conservative goals, such as reducing spending.

In addition, a few other significant measures discussed **later in this report** share the same "end-of-fiscal-year deadline" (September 30, 2023) with government funding and may be viewed as "must pass" by some lawmakers in both parties. The convergence of these issues can be expected to occupy significant time in the House, particularly in the summer and early fall.

It also is possible the Republican House might consider legislation regarding other matters as the year unfolds, perhaps including crypto currency regulation, energy infrastructure, the opioid epidemic, or even an economic stimulus package (if there is a recession). See discussion later in this report.

Hearings and investigations

House Republicans have set up investigative committees relating to such matters as the origins of the coronavirus, the economic and societal impacts of forced shutdowns, "strategic competition" between the United States and the Chinese Communist Party, and the "weaponization" of the federal government (with the last select committee having broad investigative powers to examine how the Executive Branch investigates citizens, including in criminal investigations, as well as how it collects and uses information to facilitate action against citizens).

Other investigations and proceedings might also be expected on matters relating to the IRS and unlawful disclosures of taxpayer information; the U.S. exit from Afghanistan; environmental, social, and governance (ESG) investing; the southern border; and various matters relating to President Biden and his administration. For example, the House Oversight Committee is investigating the discovery of classified documents at President Biden's personal residence as well as "suspicious activity reports" involving the business dealings of the president's son, Hunter, and the president's brother, James. Further, Rep. Fallon (R-TX) has introduced articles of impeachment against Department of Homeland Security Secretary Alejandro Mayorkas.[16]

U.S. Senate

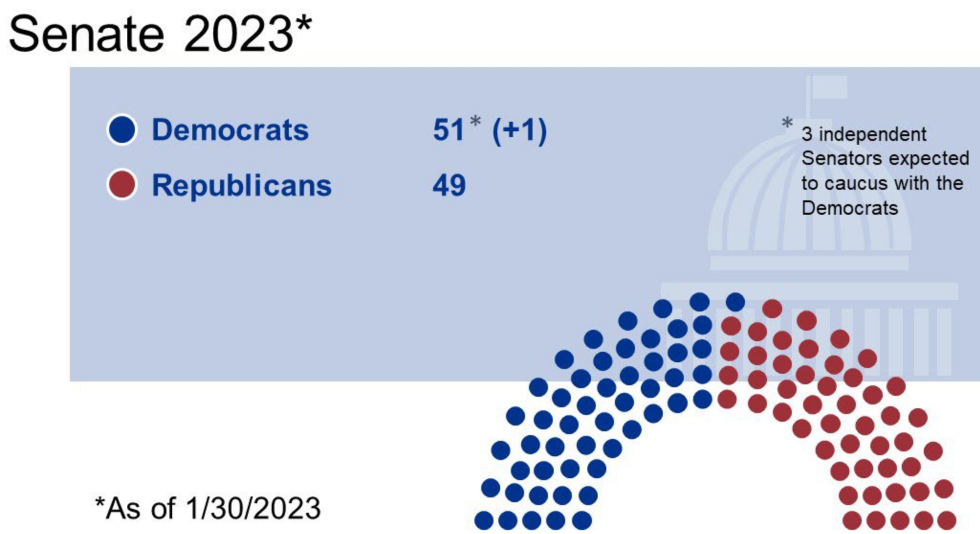
In general

The Senate convened on January 3, 2023, but recessed shortly thereafter until January 23, 2023. The Senate did not pass its organizing resolutions until early February, in large part due to a delay in finalizing membership of Senate committees.

Upon convening, the Senate consisted of 51 Democrats (including three Independents who caucus with the Democrats) and 49 Republicans.[17] On January 9, 2023, Sen. Ben Sasse (R-NE) retired. Former Nebraska Governor Pete Ricketts was sworn in to replace Sen. Sasse on January 23, 2023. Sen. Ricketts can serve until a special election is held in November of 2024 to fill the two years left in the six-year term

[15] H.R. 25 was introduced by Rep. Buddy Carter (R-GA) along with 11 other original co-sponsors on January 10, 2023.
[16] See **H.Res. 8**, which had 36 Republican co-sponsors as of January 30, 2023.
[17] The three Independents who caucus with the Democrats are: Bernie Sanders (I-VT), Angus King (I-ME), and Kyrsten Sinema (I-AZ). Sen. Sinema switched her party affiliation from Democratic to Independent on December 9, 2022. Sens. Sanders and King both have been Independents who caucus with the Democrats for many years.

to which Sasse was elected in 2020.[18] Thus, the ratio of Democrats to Republicans remains 51 to 49.



KPMG observation

In the 117th Congress, Democrats and Republicans held an equal number of Senate seats and Democrats controlled the chamber only because of the role of Democratic Vice President Kamala Harris as President of the Senate.[19] Because each party had the same number of seats, Schumer and McConnell negotiated a power-sharing agreement that, among other things, provided for committees to have equal numbers of members of each party. The agreement allowed either Schumer or McConnell to move for a Senate floor vote to approve or disapprove the release to the full Senate of legislation that received a tie vote during committee consideration.

With Democrats controlling the 118th Congress outright, a power-sharing agreement is no longer in place and Senate committees have more Democratic members than Republicans. As a result, it could be easier for Democrats to move nominations, subpoena witnesses for hearings and investigations, and move some legislative proposals through committees.[20]

As explained **later in this report**, it typically takes at least 60 votes to move legislation through the Senate. Thus, even if all 51 Democrats were to support a bill,[21] at least nine Republicans also would need to be on board for the bill to pass the Senate. Notably, some of the Republican senators who worked to build bipartisan consensus in the previous Congress are not in the current Congress—perhaps complicating the

[18] See note 5, supra regarding vacant Senate seats. Under Nebraska law, if a vacancy occurs more than 60 days before a statewide general election, the governor is allowed to appoint a replacement to serve until the start of the Congress that follows such statewide general election. See Nebraska Revised Statute 32-565.
[19] As suggested in note 17 supra, two Independents, Sens. Sanders and King, were treated as Democrats throughout the 117th Congress because they caucused with the Democrats. Sen. Sinema, however, was a registered Democrat during most of the 117th Congress (i.e., until December 9, 2022).
[20] In the 117th Congress, Republican members of committees had the ability to stall the committee's vote on a nomination simply by not showing up, thereby precluding the presence of the required quorum.
[21] As was illustrated in the 117th Congress, securing the votes of all Democratic senators for legislation that lacked Republican support could be extremely challenging, particularly given the strong preference of some Democratic senators to advance legislation on a bipartisan basis.

ability to pick up sufficient votes in some cases.[22]

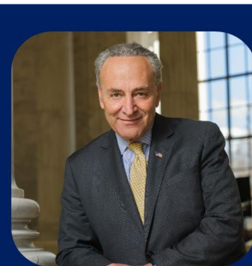
KPMG observation

Securing support from senators of both parties can be expected to involve delicate negotiations with individual senators. In past situations in which leadership of both chambers wanted to pass legislation on particular matters, the House often has accepted what the Senate has passed given concerns that any modification might upset the fragile balance of support in the Senate. It is not clear to what extent this dynamic may or may not come into play with "must pass" legislation in the current Congress given the narrow Republican control of the House and the commitments House leadership has made to give more power to rank and file members.

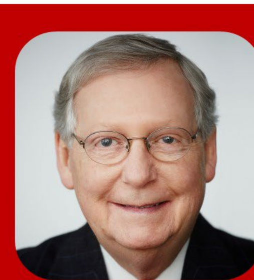
Leadership

Senate leadership for the 118th Congress remains largely the same as in the prior Congress, with Chuck Schumer (D-NY) continuing as Senate majority leader and Mitch McConnell (R-KY) remaining minority leader.

Senate leadership



Charles Schumer (D-NY)
Majority Leader



Mitch McConnell (R-KY)
Minority Leader

Possible Senate priorities

Given the need for legislation to have bipartisan support in the Senate, the Senate's legislative agenda is expected to be narrower than in the House. The Senate, however, can be expected to spend significant time on matters such as advancing administrative and judicial nominations and holding hearings.

Legislation

From a legislative perspective, the Senate can be expected to focus largely on "must pass" measures. Indeed, Senate Majority Leader Schumer already has issued multiple press releases on the need to enact debt limit legislation.[23] Building sufficient bipartisan support for "must pass" measures can be expected to take considerable time.

Further, as in the House, it is possible the Senate might consider legislation regarding other matters on which there is strong bipartisan support. (See discussion later in this report.) In addition, some moderate senators in both parties might be expected to try to build bipartisan consensus from the "center out" on some issues, much as they did successfully with infrastructure last year. For example, a bipartisan group of senators already is working to see if they can find common ground on possible legislation relating to the border and immigration.[24]

Moreover, some Senate committees might approve some legislative proposals with only Democratic votes to convey political and policy priorities, while other proposals may move through committees with significant bipartisan support (with the latter likely having a higher probability of generating the support needed to pass

[22] For example, Sen. Portman (R-OH), Sen. Blunt (R-MO), and Sen. Burr (R-NC) retired from the Senate at the end of the 117th Congress. These senators were among the 19 Senate Republicans who voted for bipartisan infrastructure legislation in 2022.
[23] Leader Schumer also issued a joint press release with House Democratic leader Jeffries. See Majority Leader's **press releases**.
[24] The group is currently being led by Sen. Cornyn (R-TX) and Sen. Sinema (I-AZ). Sen. Tillis (R-NC), a member of Senate Republican leadership, is also involved in the effort.

the full Senate on a bipartisan basis).

Nominations, hearings, and investigations

Senate Democrats can be expected to try to advance as many judicial nominations as possible, as well as the nomination of Danny Werfel to be IRS Commissioner and other administrative nominations. These nominations may take considerable time—with the nomination hearings with respect to the IRS Commissioner likely being contentious given different views regarding the activities of, and appropriate funding levels for, the IRS.

Senate committees also can be expected to hold some hearings and investigations on matters that reflect Democratic policy and political priorities or that are intended to provide "counter programming" to various House investigations. Hearings might include, for example, further investigations into IRS audits of presidential tax returns (or complicated returns of high-income individuals, in general), effective tax rates following the TCJA, and further examination of matters explored by the House "January 6" committee in the 117th Congress.

The tax-writing committees

The tax-writing committees in the House and Senate—the House Committee on Ways and Means and the Senate Committee on Finance—play key roles in the analysis, development, and drafting of modifications to the tax law. The leadership and membership of these committees can influence the substance and shape of potential tax legislation.

House Ways and Means Committee

Some of the new House rules may give the Ways and Means Committee more influence over tax legislation than in recent past years that had more leadership-driven processes. Thus, the views of the chairman and Republican members of the Committee may be even more relevant to the House's possible tax legislative agenda than in the recent past.

Chair and ranking member

Jason Smith (R-MO) is the new chairman of the Ways and Means Committee.[25] At 42 years old, he appears to be the youngest chair of the Committee ever. He has been in Congress since 2013. (Read **Jason Smith's biography** as posted on his congressional website.)

In the 117th Congress, Kevin Brady (R-TX) was the ranking Republican on the Committee. Rep. Brady had served as the committee's chairman during the 115th Congress when Republicans controlled the House, Senate, and White House and the TCJA was enacted. Former Chairman Brady did not seek re-election at the end of the last Congress.

House Ways and Means Committee

In the 117th Congress, Rep. Richard Neal (D-MA), was the chairman of the Ways and Means Committee.

[25] Two other Republican members of the Committee had also sought the chairmanship—Vern Buchanan (R-FL) and Adrian Smith (R-NE).

With Democrats in the minority in the 118th Congress, Rep. Neal now is the ranking Democrat on the Committee.

Possible priorities of new chair

With the chairmanship comes the ability to set the agenda for the Committee's focus and activities for the next two years.

At the organizing meeting for the Committee on January 31, 2023, Chairman Smith issued a **statement** indicating that the Committee would focus on among the following matters:

- Building on the successful tax reforms in the TCJA that reduced the tax burden on families and small businesses and fueled growth
- Delivering tax relief for families, farmers, and small business
- Incentivizing more domestic energy production
- Reconnecting the child tax credit to work
- Seeking accountability from the "Washington Bureaucracy" and the Biden Administration, including asking tough questions about how the Administration "wishes to use" the IRS "to snoop on Americans' finances" and "why that agency has repeatedly betrayed the trust of American taxpayers"

A few weeks earlier, in a **statement on his selection as chairman**, Smith also indicated that his priorities would include: "defunding" the "$80 billion pay increase Democrats gave the IRS to hire 87,000 new agents to target working families" in the Inflation Reduction Act; examining whether "it is in the best interests of the American people to continue showering tax benefits on corporations that have shed their American identity in favor of a relationship with China"; and using the Tax Code and trade policy to "re-shore and strengthen our supply chains."

Some of Smith's priorities in the prior Congress also might shed light on his possible current priorities. For example, in the 117th Congress, he signed on as a sponsor of a proposal to eliminate the five-year amortization requirement for R&E expenditures.[26] He also introduced bills to make permanent the child tax credit modifications made by the TCJA[27] as well as the section 199A deduction for passthrough businesses.[28] Further, along with other Republican members of the Ways and Means Committee, he signed a **letter to Treasury Secretary Yellen** [PDF 401 KB] dated December 14, 2022, characterizing the administration as having used its role in international tax negotiations to advance a "partisan political agenda."

KPMG observation

As a general matter, Chairman Smith appears to be a strong supporter of the tax cuts included in the TCJA. He also appears to be particularly interested in tax policies that help some individuals (such as working class Americans) and small businesses (including passthroughs). In the previous Congress, he reportedly indicated that revisiting the corporate alternative minimum tax (CAMT) would be a low priority if he were elected Chairman.[29]

[26] See **H.R. 1304**, the "American Innovation and R&D Competitiveness Act," as introduced in the 117th Congress. Smith was not an original co-sponsor but signed on as a co-sponsor within a month of the bill having been introduced.
[27] See **H.R. 1380**, the "Permanent Tax Relief for Working Families Act," as introduced in the 117th Congress.
[28] See **H.R. 1381**, the "Main Street Tax Certainty Act," as introduced in the 117th Congress.
[29] This statement was made at an event sponsored by Punchbowl News in December of 2022.

It is not clear to what specific corporations or tax benefits Chairman Smith was referring in his statement on being selected chairman about "showering tax benefits on corporations that have shed their American identity in favor of a relationship with China."

At the current time, it is not clear how high of a priority modifying the TCJA provision requiring amortization of R&E costs for tax years beginning after 2021 may be to the new Chairman relative to other priorities. It will be interesting to see if Chairman Smith makes any explicit statements regarding the treatment of R&E expenditures in the coming months. See discussion of extenders later in this report.

Committee membership

With Republican control of the House, there are now more Republicans on the Ways and Means Committee than Democrats. The ratio of Republicans to Democrats is 25 to 18—reversing the ratio of 25 Democrats to 18 Republicans in the 117th Congress. Ten of the Republicans are new to the committee and can be expected to bring new priorities and perspectives to the committee's agenda.[30]

Ways & Means Committee

Majority

Jason Smith, MO - Chairman

- Vern Buchanan, FL
- Adrian Smith, NE
- Mike Kelly, PA
- David Schweikert, AZ
- Darin LaHood, IL
- Brad Wenstrup, OH
- Jodey Arrington, TX
- Drew Ferguson, GA
- Ron Estes, KS
- Lloyd Smucker, PA
- Kevin Hern, OK
- Carol Miller, WV
- Greg Murphy, NC
- David Kustoff, TN
- Brian Fitzpatrick, PA*
- Greg Steube, FL*
- Claudia Tenney, NY*
- Michelle Fischbach, MN*
- Blake Moore, UT*
- Michelle Steel, CA*
- Beth Van Duyne, TX*
- Randy Feenstra, IA*
- Nicole Malliotakis, NY*
- Mike Carey, OH*

*New Committee member

Minority

Richard Neal, MA – Ranking Member

- Lloyd Doggett, TX
- Mike Thompson, CA
- John Larson, CT
- Earl Blumenauer, OR
- Bill Pascrell Jr., NJ
- Danny Davis, IL
- Linda Sánchez, CA
- Brian Higgins, NY
- Terri Sewell, AL
- Suzan DelBene, WA
- Judy Chu, CA
- Gwen Moore, WI
- Dan Kildee, MI
- Don Beyer, VA
- Dwight Evans, PA
- Brad Schneider, IL
- Jimmy Panetta, CA

KPMG observation

Because only a simple majority of the Committee is required to approve legislation, the Committee might favorably report some tax legislative proposals with only Republican support. Although such proposals may have little chance of moving through the entire legislative process and becoming law, some of these so-called "messaging bills" may pass the House and be used to publicly communicate Republican positions on certain policy issues.

The Committee also might move some tax proposals on discrete issues (such as significantly increasing the threshold for 1009-K reporting for certain transactions) with only Republican votes in

[30] The number of new members is a function of both adding Republican seats on the committee and replacing Republican members in the 117th Congress who are not in the 118th Congress. As indicated above, Rep. Kevin Brady did not seek re-election. Further, Rep. Tom Rice (R-NC) lost his primary race.

> an effort to stake out the House Republican negotiating position in case it becomes possible to add a tax title to bipartisan and bicameral legislation later in the Congress.

Senate Finance Committee

Chair and ranking member

Sen. Ron Wyden (D-OR) continues to serve as the chairman of the Senate Finance Committee, while Sen. Crapo (R-ID) continues to be the ranking Republican.

Senate Finance Committee

Ron Wyden (D-OR)
Chairman

Mike Crapo (R-ID)
Ranking Member

Committee membership

The Senate Finance Committee will consist of 14 Democrats and 13 Republicans. The Democratic members of the Committee are the same as in the 117th Congress.

Four Republican members of the Committee in the 117th Congress are not currently in the 118th Congress.[31] On February 1, 2023, Senate Republicans announced that three Republicans would join the Committee—Sens. Blackburn, Tillis, and Johnson. As a result, Democrats will have one more member on the Committee than Republicans—as compared to the last Congress in which there were 14 members of each party.

Senate Finance Committee

Majority (14)	*Minority (13)*
– Ron Wyden, OR – Chairman	– Mike Crapo, ID – Ranking Member
– Debbie Stabenow, MI	– Chuck Grassley, IA
– Maria Cantwell, WA	– John Cornyn, TX
– Bob Menendez, NJ	– John Thune, SD
– Tom Carper, DE	– Tim Scott, SC
– Ben Cardin, MD	– Bill Cassidy, LA
– Sherrod Brown, OH	– James Lankford, OK
– Michael Bennet, CO	– Steve Daines, MT
– Bob Casey, PA	– Todd Young, IN
– Mark Warner, VA	– John Barrasso, WY
– Sheldon Whitehouse, RI	– Thom Tillis, NC*
– Maggie Hassan, NH	– Ron Johnson, WI*
– Catherine Cortez Masto, NV	– Marsha Blackburn, TN*
– Elizabeth Warren, MA	

*New Committee member

[31] These four Republicans are former Senators Portman, Toomey, Burr, and Sasse. As indicated in text *supra*, Sasse retired shortly after the 118th Congress began.

KPMG observation

In the 117th Congress, committee membership was equally divided between Democrats and Republicans, with each party having 14 committee members. With a clear majority in the 118th Congress, it should be easier for Chairman Wyden to issue subpoenas, without minority support, to witnesses who might not otherwise agree to testify at committee hearings. Likewise, Democrats on the committee could advance the nomination of Danny Werfel to be IRS Commissioner to the Senate floor without Republican votes.

Having an outright majority also could allow Committee Democrats to report legislation to the full Senate by majority vote without Republican support. Nonetheless, any bills reported on a partisan basis would need to be modified (perhaps substantially) to secure sufficient Republican support to meet the 60-vote threshold and advance further in the legislative process.

It is also worth noting that, as a general matter, Senate Finance Committee members have had a history of frequent bipartisan cooperation in the tax arena.

The general legislative process

The Republican controlled House and the Democratically controlled Senate can be expected to have different legislative priorities, including with respect to major tax issues. As explained below, for any legislation to be enacted in the next Congress, the House and the Senate ultimately would have to pass the same version of such legislation before sending it to the president for his signature.[32]

House

In the House, the majority party generally controls the legislative agenda, and it only takes a simple majority to pass most legislation—other than certain tax rate increases that require a super majority vote.[33]

As a result, House Republicans can pass legislation reflecting Republican priorities with only Republican votes—assuming almost all Republican members (both conservatives and moderates) support the legislation.[34] Nonetheless, as explained later in this report, it may be challenging for the House to approve legislation on major policy issues that would also be able to pass the Senate.

Senate

Under current Senate rules, 60 votes are generally needed to avoid a filibuster of legislation. Thus, barring a change to long-standing Senate rules (a very controversial process known as the “nuclear option”), even if all 51 Democratic senators supported legislation, at least nine Republican senators also would need to be on board.[35] In other words, legislation would need significant bipartisan support to pass the Senate.

There is an alternative to the general Senate rules—known as “budget reconciliation—pursuant to which some types of legislation (including certain tax measures) can be considered in the Senate with only a

[32] Note that, under the U.S. Constitution, revenue measures (such as most tax law changes) must originate in the House. Once the House sends the Senate a revenue measure, the Senate can substantially modify the revenue provisions or even “strip and replace” the House-passed provisions with other measures. Ultimately, however, each chamber would have to pass the identical legislation before the legislation could be sent to the president for signature.
[33] See discussion of new House rules, supra.
[34] As discussed earlier in this report, House Republicans already have passed IRS “defunding” legislation without any Democratic support.
[35] As a practical matter, at least 50 Democratic senators would need to support eliminating the filibuster. There does not currently appear to be that level of Democratic support.

simple majority vote. This was the process by which the Affordable Care Act became law in 2010, the TCJA became law in 2017, and ARPA and the Inflation Reduction Act became law in the 117th Congress.[36]

Nonetheless, the use of budget reconciliation procedures to move tax legislation through the 118th Congress appears unlikely. As a threshold matter, using the budget reconciliation process would require both the House and the Senate to agree to a joint budget resolution. This resolution would create "reconciliation instructions" charging specified committees to report legislation in the form of a "reconciliation bill" that would achieve certain revenue objectives. Ultimately, the House and Senate would have to agree to identical legislation under the reconciliation process. Given starkly different policy views on many issues (relating to both spending and taxation) as well as the tight margins of control in each chamber, it is difficult to imagine the Republican controlled House and the Democratically controlled Senate agreeing to an identical budget resolution or reaching consensus on the details of budget reconciliation legislation.

Thus, any tax legislation that passes the Senate likely would need to secure at least 60 votes – i.e., it would need significant bipartisan support.

President

It is unclear at this time how President Biden will work with congressional Republicans over the course of the 118th Congress. Nonetheless, it seems likely that the White House will work with congressional Democrats (particularly in the Senate) in attempting to advance administration priorities. Further, it is possible the administration might focus its legislative initiatives on issues on which it may be able to find common ground and bipartisan support—while staking out other policy priorities as possible election issues for 2024 or beyond.

Non-tax agenda: Possible areas of bicameral agreement

Notwithstanding the significant differences between the chambers and the likely highly charged political atmosphere, House and Senate leadership might be expected to pursue legislation on some of the same matters, with the most likely areas in which bipartisan and bicameral consensus eventually might be achieved relating to legislation that typically has been considered "must pass" given the political, economic, and other potential consequences of inaction. In 2023, the primary "must pass" measures are expected to be addressing the debt ceiling and funding the government. A farm bill, FAA reauthorization, and, possibly, extending certain pandemic preparation programs also may be viewed as "must pass" by many lawmakers.

As explained below, the debt limit potentially will need to be addressed first, perhaps as soon as this June or July. For government funding, a farm bill, FAA reauthorization, and pandemic preparation, action would be needed by September 30, 2023 (the end of the 2023 fiscal year) to avoid the suspension of certain government programs and functions.

Other areas of potential bipartisan and bicameral agreement also may arise as the year unfolds. The prospects for bipartisan cooperation for other than urgent priorities might diminish by as the midterm and presidential elections in November of 2024 approach.

[36] These measures included tax provisions and were scored as *increasing* the deficit. In the more distant past, however, budget reconciliation was used on a number of occasions to enact deficit *reduction* legislation. For example, budget reconciliation acts enacted in 1990 and in 1993 were scored as reducing the deficit and included revenue increases as well as spending cuts. See **CRS Report on Budget Reconciliation Measures Enacted into Law Since 1980** [PDF 1.18 MB] (as updated on November 2, 2022) for more information on budget reconciliation legislation in the last several decades.

Debt limit

At some time in the next several months, action regarding the so-called "debt ceiling" needs to be taken to avoid a default on existing U.S. government debt obligations. Very generally, the debt ceiling is the total amount of government debt that can be outstanding under current statutory law. Eventually, if the U.S. government is unable to issue additional debt, it will be unable to meet all of its payment obligations, possibly including principal and interest payments on existing debt obligations.

The outstanding debt of the United States reached the statutory limit on January 19, 2023. Once the limit was reached, Treasury began using accounting measures to prevent the United States from defaulting on its obligations. In a **letter to congressional leaders** dated January 13, 2023, Treasury Secretary Yellen explained that, while use of so-called "extraordinary measures" enables the government to meet its obligations for a limited amount of time, that time period is subject to considerable uncertainty for a variety of factors, including challenges of forecasting payments and receipts. Nonetheless, Secretary Yellen indicated that it is unlikely that cash and extraordinary measures would be exhausted before early June.[37]

The United States has never defaulted on its debt obligations; however, it has come quite close on several past occasions (including in 2011).[38] The debt limit stakes are expected to be high and could include a steep decline in the stock market, an increase in interest rates for loans (including small business loans), inability of the government to make timely Social Security and other payments to individuals, and associated ripple effects on employment, wealth, and growth throughout the U.S. and global economies (perhaps triggering or exacerbating a recession). Some negative results (such as downgrading of government debt) might occur before an actual default to the extent credit rating agencies and markets perceive default as a real possibility.

Some Republicans have indicated that they might only support legislation increasing (or suspending) the debt limit if it is accompanied by other policy changes, such asdomestic spending cuts and substantially reducing IRS funding—changes that many Democrats strongly oppose. Significantly cutting discretionary spending could be expected to face headwinds in the Senate -- as well as from some moderate Republicans who may be concerned about possible reductions in discretionary defense spending, among other matters. Further, so far, many Democrats are generally taking the position that they will not negotiate conditions for addressing the debt limit.

It is not clear how (or when) the current impasse will be resolved. It might be necessary for the House ultimately to rely on some Democratic votes to pass legislation that can pass the Senate on a bipartisan basis but that may be strongly opposed by some conservative House Republicans. This potentially could result in a challenge to Speaker McCarthy's leadership from within the Republican caucus.

KPMG observation

Debt limit legislation sometimes has included tax provisions as part of a larger legislative measure. For example, the Bipartisan Budget Act of 2018[39] included a package of tax extenders, while the Bipartisan Budget Act of 2015[40] included substantial changes to the partnership audit rules.[41] The most recent debt limit increase (which was signed into law by President Biden on December 16, 2021), however, did not include a tax title.[42]

[37] In the past, legislation sometimes has increased the debt limit to a new dollar amount, but sometimes has suspended the debt limit for a specified period of time or if certain conditions are met (such as the adoption of a budget resolution).
[38] For a high-level history of debt limit legislation, see the Bipartisan Policy Center's "timeline" of **The Debt Limit Through the Years**.
[39] See **Pub. L. No. 115-123** [PDF 830 KB]
[40] See **Pub. L. No. 114-74** [PDF 369]
[41] Both the 2015 and 2018 bipartisan budget bills addressed government funding as well as the debt limit.
[42] See Pub. L. No 117-73 [PDF 165 KB]

Government funding

The 117th Congress enacted omnibus appropriations legislation for the fiscal year that ends September 30, 2023 (FY 2023) in late December of 2022, shortly before adjourning. The legislation included additional funding for some domestic functions and programs sought by many Democrats, as well as higher defense spending levels supported by many Republicans. Most House Republicans, including House Republican leadership, did not participate in the negotiations, with some preferring to extend previous funding levels until Republicans took control of the House.

Because the omnibus legislation only addressed appropriations through September of 2023, funding for government agencies and functions would need to be enacted again for the next fiscal year (FY 2024) before October 1, 2023, to prevent a government shutdown. Because yet another fiscal year (FY 2025) will begin on October 1, 2024 (shortly before the November 2024 elections), the 118th Congress also would need to address government funding for at least part of FY 2025 at some point as well. Technically, the government could be funded either by enacting appropriations legislation for various government agencies and functions or, as often happens, by extending existing funding levels for some or all functions through one or more continuing resolutions.

Reaching bipartisan and bicameral agreement on government funding can be expected to face substantial challenges given substantially different views as to appropriate funding levels for various functions both between Republicans and Democrats in general, and between more conservative and more moderate Republicans on certain issues. Moreover, as with the debt limit, it is possible that reaching agreement on legislation that could pass the Senate with at least 60 votes might need to rely on Democratic support in the House, potentially leading to a vote to replace McCarthy as speaker.

Given these challenges, it would not be surprising for there to be one or more government shutdowns during the 118th Congress. It is also quite possible that the IRS might be one of the few functions relatively unaffected if there were a shutdown because of the long-term funding already appropriated to it by the Inflation Reduction Act.[43]

KPMG observation

Government funding bills (such as omnibus appropriations bills and continuing resolutions) have been vehicles for tax provisions on many occasions in the past. For example, the omnibus appropriations legislation enacted at the end of 2022 included tax provisions relating to retirement savings (with a revenue offset limiting tax deductions for charitable contributions of conservation easements in certain situations). Notably, however, the 2022 omnibus did not address tax extenders (including some scheduled changes that had gone into effect at the start of 2022). Tax extenders are addressed **later in this report**.

Farm bill, FAA reauthorization, and pandemic response legislation

Several other authorization bills "expire" on the same date as government funding (September 30, 2023) and might be considered "must pass" by many Republican and Democratic lawmakers. Given the confluence of timing, some of the political and policy issues associated with these measures might be negotiated concurrently with government funding legislation. It is possible, but far from certain, that compromise legislation on some or all the issues might be packaged together in one comprehensive measure.

[43] The **contingency plan the Treasury Department released in September of 2022** [PDF 186 KB] (during the last Congress) suggests that a shutdown might not affect normal IRS operations because of the additional funding the IRS received through September 20, 2031 for all IRS appropriation accounts in the Inflation Reduction Act.

Farm bill

The current agricultural authorizations act (i.e., the “farm bill”) was enacted in 2018 and provides funding for a wide array of programs through the end of the current fiscal year.[44] Programs funded by the legislation relate to matters such as crop supports, crop insurance, conservation, energy, agricultural research, commodities, trade, forestry, horticulture, rural development, and nutrition. The largest share of funds goes to the Supplemental Nutrition Assistance Program (SNAP).[45]

Enacting a new farm bill (or, at least, extending prior legislation) is likely to be a high priority for some lawmakers in both parties and to be considered “must pass” by various stakeholders.[46] Nonetheless, reaching bipartisan and bicameral consensus on all the different programs funded by the bill could be very challenging given the wide array of competing views on particular programs; political and ideological differences; different interests of different stakeholders; and different state, regional, and local perspectives.

KPMG observation

The most recent farm bills have not included tax titles. However, a farm bill enacted in 2008 included a fairly robust tax package with provisions relating to conservation, timber REITs, energy, agriculture, race horse depreciation, and other matters, along with revenue-raising provisions.[47]

FAA reauthorization

Spending authority for the FAA and several excise taxes dedicated to the Airport and Airways Trust Fund are scheduled to expire at the end of FY 2023 (i.e., on September 30, 2023).[48] Congress would need to reauthorize FAA programs and funding by that date to avoid a furlough of nonessential FAA employees and airport construction workers and to continue to collect the airport and airway related excise taxes.

Enacting FAA reauthorization legislation has faced some challenges in the recent past. In 2017, for example, reauthorization legislation[49] was enacted just a day before a partial shutdown would have occurred due to differences on various nontax issues (such as efforts by some lawmakers to privatize certain functions).[50] The following year, a five-year reauthorization of FAA programs and funding was enacted—making further authorization unnecessary until the end of FY 2023.

KPMG observation

FAA reauthorization legislation typically includes extensions of the airport and airway related excise taxes. In situations in which FAA reauthorization legislation has been enacted on a stand-alone basis (as opposed to being folded into a larger legislative vehicle), the tax title has often been limited to the aviation related excise tax provisions. Note, however, that the FAA reauthorization

[44] The Agriculture Improvement Act of 2018 (Public Law No. 115-34).
[45] SNAP, commonly called “food stamps,” is described by the Food and Nutrition Service of the Department of Agriculture as supplementing “the food budget of needy families so they can purchase healthy food and move towards self-sufficiency.” See **Supplemental Nutrition Assistance Program (SNAP)**
[46] If a new bill is not enacted, and the 2018 legislation is not extended, by the end of September of 2023, dairy support pricing might revert to that provided in older legislation, potentially resulting in increased prices for some products.
[47] See Title XV (Trade and Tax Provisions) of the “Food, Conservation, and Energy Act of 2008), **Pub. L. No. 110-234** [PDF 1.65 MB]
[48] These excise taxes include: the tax rates on noncommercial aviation kerosene and noncommercial aviation gasoline (except for the permanent 4.3-cents-per-gallon rate); the domestic and international air passenger ticket taxes and the ticket tax exemption for aircraft in fractional ownership programs; the air cargo tax; and the surtax on fuel used in aircraft in fractional ownership programs.
[49] The Disaster Tax Relief and Airway Extension Act of 2017 (**Pub. L. No. 115-63** [PDF 274 KB]) was passed by the House on September 25, 2017, was passed by the Senate with an amendment to which the House agreed on September 28, 2017, and was signed into law on September 29, 2017.
[50] According to news reports at that time, the potential shutdown was not expected to result in flight cancellations, but the government would have lost revenue from not being able to collect the airport and airways excise tax if a shutdown had occurred.

legislation that was enacted in 2018 also included a package of disaster tax relief provisions in response to Hurricanes Harvey, Irma, and Maria.[51]

Pandemic preparedness

The "PREVENT Pandemics Act" authorizes a variety of programs regarding medical and public health preparedness, research, and response to existing and emerging health threats for the fiscal year ending September 30, 2023. The legislation initially was introduced by Sens. Murray (D-WA) and Burr (R-NC) in March of 2022. Shortly thereafter, it was favorably reported by the Senate Health, Education, Labor, and Pensions (HELP) Committee on a bipartisan vote of 20 - 2. Several months later, much of the bill was incorporated into the omnibus appropriations legislation that was enacted at the end of 2022.

Other possible bipartisan measures

It is possible that Republicans and Democrats might be able to reach bipartisan and bicameral agreement on some issues on which they might not have starkly different policy views (such as cryptocurrency regulation, the opioid epidemic, energy infrastructure, and online privacy protection) – assuming differences over other matters do not "poison the waters" and stifle the ability to cooperate on less divisive issues.

New high priority issues related to future events that are unknowable at the present time also could develop that could drive a bipartisan legislative response. In the past, for example, recessions and financial market disruptions have resulted in significant bipartisan legislation. Nonetheless, reaching bipartisan and bicameral agreement on the substance of such legislation could face the same challenges described above given the likely different views by different members as to the appropriate legislative response.

Possible tax agenda

Given the general challenges expected to be associated with enacting legislation during the 118th Congress, tax professionals will need to consider which bills are mainly meant to communicate political priorities and which might have sufficient bipartisan and bicameral support to become law. Moreover, even for tax proposals that can garner significant bipartisan support, there is a question as to whether there is a legislative vehicle to which they could be attached that might make it through the entire legislative process.

The discussion addresses these issues as well as other frequently asked questions about the federal tax legislative outlook for the divided Congress.

What appear to be the most likely vehicles for bipartisan tax law changes?

Given the limited number of bills that might be able to make it through both the House and the Senate, tax professionals would be well advised to watch *any* bill that appears to have enough bipartisan and bicameral support to move through the entire legislative process for the possible inclusion of tax provisions.

Nonetheless, as a very general matter, the narrower the scope of a bill, the narrower the scope any tax title that might be included is likely to be.[52] Thus, any tax provisions that might end up being included in a bill on a discrete topic (such as cryptocurrency, farming, or energy infrastructure) stand the best chance of

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[51] See the staff of the JCT's general explanation of legislation enacted in the 115th Congress (JCS-2-19) for a summary of the tax provisions included in the 2017 FAA reauthorization legislation.

[52] Including unrelated tax provisions in a bill that addresses a relatively narrow topic can raise questions of germaneness; can complicate the negotiations; and, in some cases, can make reaching bipartisan consensus on the scope and substance of the overall legislation more difficult.

being focused on the particular issue areas addressed by the underlying legislation. (See later in this report for more on this topic.)

By contrast, tax provisions with broad application may have a better chance of being added to legislation that addresses a wide range of issues or the economy overall—such as government funding, debt limit legislation, or a comprehensive bill addressing several of the end-of-FY-2023 matters. Indeed, adding extraneous measures, like tax provisions, to "must pass" legislation sometimes can help attract needed support for the overall legislation. Nonetheless, it may be harder to attach tax provisions to debt limit or government funding legislation in the current Congress than in the past. For example:

- Reaching bipartisan and bicameral consensus on the underlying legislation itself may be extremely difficult, even before layering in a need to reach consensus on a possible tax package.

- It is possible that tax issues on which bipartisan consensus might be achievable might not be a sufficiently high priority given the major nontax issues in play.

- It is also possible that negotiations regarding tax provisions could become too politically charged for bipartisan and bipartisan consensus to be reached. For example, to the extent some Republicans demand that significant spending cuts (and, possibly, changes to entitlement programs) be included in "must pass" legislation, some Democrats might assert that increasing taxes on high income individuals and closing perceived loopholes should also be on the table. Given different views both on tax policy, in general, and on how some tax law changes affect the deficit, negotiating on *any* tax issues being included in such measures might be a nonstarter.

Thus, while debt limit and government funding bills may be the most likely vehicles for tax provisions of broad application, whether any tax provisions ultimately might be included in these measures is uncertain.

What kinds of tax legislation might (or might not) be enacted this Congress?

Given the composition of the 118th Congress, enactment of legislation making *major* tax policy changes currently appears unlikely given starkly different views of various Democratic and Republican lawmakers on significant tax issues.[53] Instead, the direction of tax policy appears more likely to become a campaign issue going into the 2024 congressional and presidential elections. For example:

- Although the House might pass legislation to extend the temporary changes made by the TCJA to the individual rate structure and to deductions for individuals beyond their scheduled expiration at the end of 2025 (during the *next* Congress), it is unlikely such a measure would pass the Senate and be signed into law in this Congress.[54]

- Although the House might vote on the Fair Tax Act (which proposes to replace the income tax and certain other taxes with a national sales tax), the bill might not have sufficient support to pass the House and, even if it does, the bill appears to have virtually no chance of advancing through the Senate.

- Although Senate Finance Committee Chairman Wyden might continue to propose some tax policy changes supported by progressive Democrats and might try to move some proposals through the Finance Committee with only Democratic support, partisan proposals may have little chance of passing the full Senate, much less the House.

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[53] There is a remote possibility a "grand bargain" to increase taxes in exchange for reducing spending could be reached. Nonetheless, although such deals were made decades ago, it seems highly unlikely at the current time that such an agreement could be reached in the highly polarized political environment.

[54] Temporary provisions in the TCJA include: the rate structure, the increased standard deduction, the cap on the deduction for state and local taxes, the section 199A deduction against business income earned through passthrough entities, and the increased estate, GST, and gift tax exemption amount.

- The increases in the income tax rates on corporations and higher income individuals proposed by the Biden Administration during the 117th Congress as part of the "Build Back Better" initiative[55] appear to have little chance of becoming law in the 118th Congress.

Nonetheless, *some* tax law changes may have sufficient bipartisan support to be able to pass both chambers of Congress and be signed into law by President Biden, assuming there is an appropriate legislative vehicle. At the current time, for example:

- The airport and airway excise taxes might be expected to be extended in FAA reauthorization legislation.

- If Congress addresses some discrete policy issues on a bipartisan and bicameral basis, it is possible that some relatively noncontroversial tax law changes on particular tax issues that fall within the scope or "theme" of the larger bill may be included. These kinds of changes may be of interest to particular industries or sectors. For example, it is possible that tax provisions related to energy infrastructure might be included in an energy infrastructure bill or that agriculture or conservation related tax provisions might be included in a farm bill.

- It is possible that some relatively discrete and noncontroversial matters where there are not big policy differences between more conservative and more progressive members of Congress might be included in "must pass" legislation, assuming the obstacles to such legislation including a tax title are surmounted.

- Non-controversial procedural changes also might be added to a larger bill, as well as issues of interest to particular members of Congress that are not sufficiently controversial to derail bipartisan support for the overall bill.

It also is possible that some tax issues might become priorities in response to future events and developments (such as possible economic "shocks" or some sort of national or international crisis)—much as COVID-19 spurred tax legislation that had not been anticipated before early 2020. For example, if there is a recession, it is not beyond the realm of possibility that significant tax components with bipartisan support might be included in a possible stimulus package. Nonetheless, navigating policy and political disagreements over matters such as the balance of tax incentives for businesses relative to individuals could prove to be a high hurdle.

See separate discussions below regarding whether legislation addressing tax extenders or the taxation of multinational businesses might successfully move through the legislative process.

What about tax extenders?

The Tax Code includes some tax incentives with scheduled expiration dates, as well as some provisions with modifications that are scheduled to take effect as of certain dates (collectively, "tax extenders").[56] For many years, Congress has extended most expired or expiring tax incentives fairly routinely, sometimes prospectively but sometimes retroactively, and without offsetting the revenue costs as scored by the JCT. Recently, however, the legislative landscape regarding tax extenders has become more complicated as certain provisions that were enacted on a partisan basis have joined the list of provisions viewed as tax extenders by many lawmakers.

Specifically, the TCJA included several provisions that were scheduled to be modified, or to take effect, on specified future dates in order to raise revenue to offset the costs of taxpayer-favorable changes made by

[55] Read ***TaxNewsFlash*** [PDF 1.38] for KPMG observations and analysis regarding the tax proposals in the Biden Administration's budget for FY 2022. Read ***TaxNewsFlash*** [PDF 2.49 MB] for KPMG's observations and analysis regarding the "Build Back Better" tax proposals that passed the Democratically controlled House in November of 2021.
[56] See **JCX-1-23** for a list of expiring tax provisions that was issued by the staff of the Joint Committee on Taxation ("JCT") on January 18, 2023.

the legislation (such as the reduction of the corporate income tax rate). The TCJA also included some favorable provisions (such as reductions in individual income tax rates) that were scheduled to phase out or sunset on specified dates. These scheduled changes allowed the legislation to satisfy scoring requirements associated with the budget reconciliation procedures that were used to advance the legislation through the Senate with only Republican votes.

KPMG observation

Some of the TCJA's scheduled changes already have become effective. For example, the provision that requires amortization of research and experimentation (R&E) expenditures under section 174 became effective for tax years beginning after December 31, 2021, as did a change to the formula for determining the limit on business interest expense deductions. Further, a scheduled phase-out of bonus depreciation begins for property place in service in 2023.

In addition, in the 117th Congress, Democrats included a temporary expansion of the child tax credit in ARPA, which was enacted on a partisan basis using budget reconciliation procedures in March of 2021. The expanded credit did not include a work requirement and was refundable and advanceable (such that recipients included payments throughout the year). The expanded credit expired at the end of 2021. The extended expansion was not included in the Inflation Reduction Act that was enacted later in the 117th Congress with only Democratic votes.

As the end of 2022 approached, some businesses were focused on whether a package of tax extenders that addressed time sensitive TCJA provisions (such as the change in treatment of R&E expenditures) would be included in the omnibus appropriations legislation that ultimately was enacted in December of 2022. Some Democrats wanted some sort of expanded child tax credit to be included in any tax extenders package—particularly if the package otherwise would primarily benefit businesses and would remove or postpone provisions used to offset the cost of the TCJA's corporate income tax rate reduction.

Ultimately, Republicans and Democrats were not able to agree to a deal on the substance of a tax extenders package and tax extenders were left out of the year-end bill.

KPMG observation

For a discussion of possible reasons why tax extenders were not included in the end-of-2022 legislation, listen to a **KPMG *Catching Up on Capitol Hill* podcast**.

The outlook for tax extenders legislation in the 118th Congress remains uncertain. Including a tax extenders package in a legislative vehicle that has the bipartisan and bicameral support necessary to become law would require successfully navigating challenges discussed earlier in this report, as well as clearing other hurdles. For example:

- As **discussed above**, debt limit legislation and government funding legislation currently appear to be the most likely potential vehicles for tax extenders. However, it is not clear how high of a priority tax extenders might be compared to the major nontax policy issues potentially in play (such as spending cuts, entitlement changes, immigration, and abortion).

- It also may be politically challenging to include tax extenders in legislation that might include spending cuts to achieve some measure of deficit reduction, particularly if the revenue costs of tax extenders are not offset (as is typically the case).

- Consensus would have to reached on the substance of a tax extenders package and whether some form of enhanced child tax credit would be included. Although House Republicans might have more leverage in negotiations than in the 117th Congress, reaching bicameral and bipartisan consensus on what, if any, enhancements to the child tax credit should be available could continue to be a thorny issue—with some Senate Democrats perhaps viewing an enriched child credit as critical to an extenders package they may otherwise view as heavily business oriented, particularly if Republicans are demanding significant cuts to domestic spending programs.

Difficult issues also may be faced in addressing the effective date of scheduled tax law changes that already have taken effect, including the changes to the treatment of R&E expenditures and to the business interest expense limitation. These issues could become more complicated to the extent legislation addressing tax extenders is not enacted by the extended due dates for 2022 tax returns.

Thus, while there may be a path for extenders to move forward at some point this Congress, the legislative landscape for extenders remains murky. In addition, even if a package of tax extenders is attached to "must pass" legislation, such legislation might not be enacted until summer or fall at the earliest.

Might legislative changes to the U.S. taxation of multinational businesses be on the horizon?

Given the policy differences between Democrats and Republicans on major tax issues (including the taxation of multinational businesses) as well as the difficulties expected to be associated with reaching agreement on legislation in general, enacting significant changes to the taxation of multinational businesses during the 118th Congress appears unlikely at the present time.

Some have queried whether a recent directive on a minimum tax adopted by European Union (EU) member countries, and the adoption of the Organization for Economic Cooperation and Development (OECD) minimum tax proposal elsewhere, might increase the likelihood of bipartisan cooperation on legislative changes to some aspects of multinational tax rules in this Congress. Nonetheless, as explained below, Republican taxwriters currently do not support the legislative responses that have been advocated by the Administration and by many congressional Democrats. Further, neither party may view working together to reach some sort of bipartisan agreement within the next two years to be a critical priority. And, even if some sort of agreement could be reached on substance, there would still be thorny questions as to whether a tax package could be attached to a legislative vehicle, such as government funding, that already faces many challenges. (See **discussion of potential vehicles** above.)

Background

During the 117th Congress, the Biden Administration proposed a number of major tax policy changes to the taxation of multinational businesses,[57] while also engaging in international negotiations with other members of the OECD on a two-pillar approach to reforming current agreed international tax rules and standards.[58] Some of the administration's legislative proposals aligned with, and were informed by, the policy objectives of the OECD work (although certain design features varied). Legislative proposals included revising the global intangible low-taxed income (GILTI) rules and replacing the base-erosion anti-abuse tax ("BEAT") with a different regime. These legislative changes, however, were not included in the Inflation Reduction Act or other legislation enacted in the 117th Congress.

In December of 2022, European Union (EU) member states agreed to a directive providing for the adoption of a 15% minimum tax based on financial statement income for certain large multinational businesses based on the second pillar of the OECD approach. Under the directive, a country that adopts the minimum tax would be able to impose a "top-up" tax on a company operating in its jurisdiction if the business's home country does not tax its profits at a rate of at least 15% under a compliant regime. EU members states have until December 31, 2023, to transpose the directive into legislation, with the top-up tax generally not

[57] For more information, read the **KPMG report** [PDF 1.38 MB] on the tax proposals in the administration's fiscal year 2022 budget.
[58] Very generally, the first pillar of the OECD initiative would provide "market jurisdictions" a new taxing right that goes beyond the arm's-length principle and permanent establishment standard, while the second pillar relates to a global minimum tax regime that is intended to ensure that all internationally operating businesses pay at least a minimum level of tax on their income in each jurisdiction regardless of where they are headquartered or the jurisdictions in which they operate.

starting to apply until after 2024.

Thus, even if implementation of the directive goes smoothly and the U.S. minimum tax regime is not determined to be compliant with the directive, U.S. multinationals likely would not be subject to the top-up tax or other adverse tax measures in the EU until after the 118th Congress ends. Thus, the potential top-up tax might not become a priority of this Congress.

For more information on the EU directive, as well as information on OECD negotiations, read ***TaxNewsFlash-BEPS***.

Political response, so far

In the 117th Congress, Republican members of the House and Senate tax-writing committees (along with other Republican lawmakers) expressed concerns about both the EU directive and the Biden Administration's role in negotiations with OECD and EU member states.

For example, in a **letter to Treasury Secretary Yellen** [PDF 401 KB] dated December 14, 2022, Sen. Jim Risch (R-ID), the ranking member of the Senate Foreign Relations Committee, along with Republican members of the tax-writing committees, characterized the administration as having used its role in international tax negotiations to advance a "partisan political agenda" and stated that, while "foreign countries, and even Treasury, have threatened that U.S. companies will be subject to foreign tax under [the agreement], Congress has shown united opposition to extraterritorial taxes in the past …." [59] Jason Smith, the current chairman of the House Ways and Means Committee, was one of the signatories to that letter.

Thus, absent unforeseeable future events, reaching bipartisan and bicameral agreement on substantial changes to the taxation of multinational businesses appears unlikely in this Congress.

What about technical corrections?

While it is possible that some technical corrections to prior tax legislation might be included in bipartisan legislation that becomes law, such an outcome is far from certain.

As a threshold matter, it is not clear that a tax technical corrections package would have the depth or breadth of support needed to be added to a legislative vehicle, such as debt limit or government funding legislation. Indeed, at the current time, it is not clear how important enacting technical corrections legislation may be to the chairs and members of the House and Senate tax-writing committees relative to other priorities.

Further, technical corrections to budget reconciliation legislation that was enacted on a partisan basis may face some political headwinds—although is possible that concerns about technical corrections to the TCJA or the Inflation Reduction Act might be mitigated to some extent by pairing corrections to both laws in the same bill.

What about IRS funding?

Although not a tax issue *per se*, IRS funding can be expected to be a recurring political issue throughout the 118th Congress.

As a general matter, many Republicans in both the House and Senate can be expected to continue to propose substantial reductions in IRS funding (as well as limits on how funding can be used) in either stand-

[59] Also in the 117th Congress, then Ways and Means Committee ranking member, Kevin Brady (R-TX) and Rep. Kevin Hern (R-OK), wrote Secretary Yellen a **letter** [PDF 166 KB] dated October 27, 2022, describing earlier efforts to provide information with respect to the first pillar of the OECD agreement (including information about what jurisdictions, on net, would be gaining or losing taxing rights) and requesting that the Treasury preserve all relevant documents.

alone legislation or as part of larger "must pass" legislation. Indeed, the House has already passed legislation to substantially carve back the funding provided by the Inflation Reduction Act as its first order of legislative business. Further, the House Ways and Means Committee plans various oversight hearings related to the IRS, with Chairman Smith having characterized Democrats as "hell-bent on supercharging" the IRS against the middle class. Read Chairman Smith's **statement**

By contrast, most Senate Democrats can be expected to strongly oppose efforts to substantially reduce IRS funding. Senate Majority Leader Schumer, for example, issued a **statement** characterizing the House bill as a "giveaway to multi-millionaires and big corporations." Likewise, Finance Committee Chairman Wyden issued a **press release** describing the additional funding provided by the Inflation Reduction Act as intended to address "a decade of Republican budget cuts" that "gutted the IRS's ability to crack down on cheating by wealthy individuals and big corporations" and that "hobbled customer service for the vast majority of families and small businesses who follow the law." The Finance Committee also might be expected to hold hearings highlighting difficulties the IRS faces in examining complicated returns of high-income Americans and the possible lack of compliance by some businesses and individuals.

All in all, it appears unlikely that the Democratically controlled Senate ultimately would agree to scale back the IRS funding provided by the Inflation Reduction Act to the substantial extent proposed by House Republicans. Nonetheless, there is a possibility that Senate Democrats may agree to *some*, much lesser, reduction of IRS funding as part of negotiations over must pass legislation – with the larger issue of the appropriate size and focus of the IRS remaining an election issue.

What about the nomination of a new IRS Commissioner?

The Senate Finance Committee and the full Senate are expected to consider the nomination of Danny Werfel to be Commissioner of the Internal Revenue Service. The starting date for hearings on the nomination, however, has not yet been announced.

KPMG observation

The nomination process can be expected to be politically charged, not necessarily because of the nominee himself but because of different views about the role and activities of the IRS.

What about tax treaties?

It is not clear whether the impasse that has caused a long delay in Senate approval of a number of pending tax treaties in prior Congresses will be broken in the 118th Congress.

A number of tax treaties continue to await Senate approval but have been put on "hold" by Sen. Rand Paul (R-KY), who continues to serve in the 118th Congress. Tax treaties pending before the Senate include agreements with Chile, Hungary, and Poland.

Note that a treaty and protocol with Vietnam was signed in 2015, and a treaty with Croatia was signed in December 2022, but neither has been transmitted by the Administration to the Senate yet. Also note that the United States notified Hungary on July 8, 2022, of the termination of the existing U.S.-Hungary income tax treaty. The termination date was effective on January 8, 2023, with the income tax treaty ceasing to have effect for withholding taxes on January 1, 2024. For other taxes, the treaty ceases to have effect with respect to periods beginning on or after January 1, 2024.

Will there be a "Bluebook" on legislation enacted in the previous Congress?

Within the next few months, the staff of the Joint Committee on Taxation (JCT) might release one or more general explanations of tax legislation enacted in the 117th Congress, such as the Inflation Reduction Act. The JCT staff often releases a general explanation (a "bluebook") of significant tax legislation that either addresses a specific piece of tax legislation or that covers numerous pieces of tax legislation enacted during a particular Congress. Release of a blue book addressing the Inflation Reduction Act could be helpful to taxpayers in better understanding the corporate alternative minimum tax (CAMT) and other provisions in that legislation, as well as to Treasury as it continues to implement the legislation.

Note that, although blue books can be relevant in interpreting a law, they do not constitute official legislative history. See, e.g., *United States v Woods,* 134 S.Ct. 557 (2013).

Resources

Stay tuned to ***TaxNewsFlash-Legislative Updates*** for developments relevant to potential federal tax legislation.

Listen to ***Catching Up on Capitol Hill* podcasts** for insights from KPMG tax professionals on what's happening in Washington on trending tax issues and what might happen next.

Contact us

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