



In this issue:

Still no clarity on details, timing of slimmed-down Build Back Better package.....	1
Deloitte Tax alert looks at new guidance on domestic passthrough entities owning stock in foreign corporations.....	5
Ways and Means Oversight subcommittee hearing to examine taxpayer problems with IRS.....	6

Still no clarity on details, timing of slimmed-down Build Back Better package

West Virginia Democratic Sen. Joe Manchin reiterated this week that he will not support an expansive Build Back Better package and that any legislation Congress eventually sends to President Biden must be narrower and more focused than the measure that cleared the House last November. But even though the White House and congressional Democratic leaders have acknowledged that the tax-and-spending bill will have to be substantially modified to address Manchin’s concerns, precise details of just what a revised proposal might look like and when it might come to the floor in either chamber remain elusive.

Here are some observations from Deloitte Tax LLP’s Tax Policy Group leaders on the status of Build Back Better negotiations, the other significant priorities facing Congress that may be competing with that legislation for floor time, and the prospects for getting a bill of some kind to President Biden’s desk this year.

What does Manchin want?

Talking to reporters at the Capitol this week, Sen. Manchin declared Build Back Better “dead,” although he subsequently clarified that he was referring only to the roughly \$1.75 trillion House-passed legislation and that he remains open to a smaller package depending on what Democratic party leaders put forward. (“We’ll see what people come up with,” he said.)

Since he announced late last year that he opposes the House measure in its current form, Manchin has been vocal in stating what he dislikes about that legislation but has been less forthcoming with a definitive list of provisions that he *would* support. (Reportedly he at one point provided such an outline to the White House but since has indicated that it no longer reflects his thinking.)

Comments he made on February 1 did little to clarify his position.

“I just want to make sure that we find a balance,” he told reporters. “And something we can afford and do it right. Whatever we do. The bottom line is to be able to pay for it and be honest with the American people.”

Other high-profile issues crowding the stage

Build Back Better seems to be on pause right now as other issues are center stage in Congress—notably, work on an omnibus spending bill for FY 2022, legislation to promote domestic high-tech manufacturing capabilities and address concerns around competition with China, negotiations over updating the Electoral Count Act, filling the upcoming vacancy on the Supreme Court, and a possible response to Russia-Ukraine tensions. But it would be hard to see Democrats walking away from a high-profile legislative priority such as Build Back Better, especially given the fact that they have pre-loaded the system with the powerful tool of budget reconciliation, which clears procedural hurdles in the Senate and potentially allows Democrats to get a bill across the finish line in that chamber without having to rely on Republican support.

Challenges focused largely on the spending side

Most of the challenges Democrats face are over how to spend money to support the president’s social priorities, not how to raise it, the inverse of what we usually see. This is not to say there is no controversy when it comes to a potential tax title for Build Back Better; however, proposals to raise tax revenue are not the primary source of Democrats’ angst.

Here are some of the main tax provisions yet to be resolved, which are all on the incentive side of the ledger:

- Enhancements to the refundable child tax credit;
- Discrete issues in clean energy, such as whether to provide “bonus” credits for union-made electric vehicles and the appropriate percentage to allow for certain direct-pay provisions; and
- Proposals (mainly from “blue state” Democrats) to relax the current-law cap on the deduction for state and local taxes.

Concerns over inflation

Sen. Manchin's main objections are broader than tax and they start with the overall size and scope of the package and its potential impact on inflation and the national debt. Inflation numbers for January are coming out on February 10 and may influence the pace at which he wants to re-engage with his colleagues on Build Back Better.

Fewer spending programs, longer timelines

Some progressive Democrats have not yet conceded the changes that likely must be made to Build Back Better. Sen. Manchin has said that lawmakers' reliance on short-term spending provisions and tax incentives in the House-approved package masks the true cost of the bill since a future Congress likely would try to extend these provisions or make them permanent. So the path to success seems obvious to many—that is, jettison the plethora of short-term spending programs that sunset or phase out after just a few years and instead offer fewer programs that are funded over the full 10-year budget window.

Indeed, President Biden acknowledged as much when he stated in a recent press conference that the best path forward is to “break the package up, get as much as we can now, and come back and fight for the rest later.” And Senate Majority Leader Charles Schumer, D-N.Y., endorsed that strategy when he told reporters February 1 that “[w]e want to get as much of Build Back Better as we can, and you will see us move forward on it.”

The winnowing-down process may not be simple, however. Restructuring the bill to address Manchin's concerns will be painful for those who are championing provisions that get left behind and who will receive in return little more than a promise from leadership to try to include them in subsequent legislation.

Deadline? What deadline?

The only real deadline for passing legislation attached to the FY22 reconciliation vehicle is the end of September, when the FY22 budget resolution containing the original reconciliation instructions expires. In past reconciliation efforts, the Senate has almost always had a real backstop—such as the August, Thanksgiving, and Christmas recesses—to force its members to make decisions and take action on difficult legislative issues. But those potential deadlines are all in the second half of the calendar year, and Democrats surely can't afford to wait that long and still deliver Build Back Better to the White House.

Instead, many Democrats—particularly those in the party's progressive wing—have hoped to turn the president's State of the Union address on March 1 into an action-forcing event, although so far Sen. Manchin seems unenthused about being pressured to come to decisions here. Success for Democrats on Build Back Better would be much more likely if there is at the very least a clear framework, if not an actual agreement with Sen. Manchin, by March 1.

A lurking concern for Democratic leaders remains the slim margin of their majority, something brought into stark focus by this week's revelation that New Mexico Democratic Sen. Ben Ray Lujan is in the hospital recovering from a stroke and subsequent surgery to relieve swelling in his brain. It is unclear just how long it will be before Lujan is back on Capitol Hill (press reports, citing comments from Lujan's aides, are suggesting four to six weeks) but his expected absence from the Senate floor casts further doubt on whether Build Back Better can pass in some form in the near term, since even if Manchin gets on board with a compromise package, Democrats won't be able to approve anything on a party-line basis until Lujan returns. (See additional discussion below on outside factors that could alter the congressional legislative agenda.)

Could failure on voting rights or success on a SCOTUS nomination fuel a Build Back Better rally?

There are some similarities between the difficulties facing Democrats in moving Build Back Better legislation and the failed effort by the GOP to repeal and replace the Affordable Care Act in 2017. When Republicans were unable to repeal the Affordable Care Act, they subsequently rallied around the Tax Cuts and Jobs Act as something important they could pass.

This raises the question of whether last month's failure by Senate Democrats to change the filibuster rules as they apply to voting rights legislation could lead to a similar pivot to Build Back Better as a high-profile priority that the party can embrace. To be sure, there are important differences in the politics, policy, and personalities of the players this time around, and the immediate priority for Democrats in 2022 appears to be the coming Supreme Court vacancy and not Build Back Better. In that regard, a successful confirmation effort could also create some Democratic unity that could spur a revival of Build Back Better legislation. While not complete parallels, there are similarities to 2017 worth keeping in mind as we think about whether Democrats will have the drive to rally around a revised version of Build Back Better, even if that product falls short of what some members hoped to pass.

Prospects for expired provisions

So far, there do not appear to be any imminent plans to deal with expired tax provisions, including many clean energy provisions that are addressed in the House-passed version of Build Back Better, as well as the now-in-force changes regarding the treatment of research expenditures under section 174 and limitations on deductions for interest expense under section 163(j). It is not impossible that they could ride on a larger omnibus spending package, which is currently being negotiated by appropriators and congressional leadership; however, it doesn't currently appear that an agreement on an omnibus will be in place by February 18, when the current continuing resolution funding government operations expires. That means another temporary funding patch is likely, and those rarely carry extraneous provisions like tax code changes. Congress has a habit of addressing extenders retroactively and there is little reason to think lawmakers will take a different approach this year. If Build Back Better is not revived, there is a small possibility that a section 174 suspension could catch a ride on the China competitiveness legislation currently moving through Congress, and we will be watching that closely in the coming weeks.

Beware the ‘black swan’

Sometimes, the best laid plans in Congress get upended by unforeseen “black swan” events. Already on the horizon are three potential agenda-busters: the situation with Russia and Ukraine; the looming retirement of Justice Breyer and Democrats’ plans to quickly fill his seat; and the continued threat of new COVID variants, their impact on economy, and the possible need for additional fiscal support. Any of these could refocus the attention of Congress and the White House and continue to relegate Build Back Better to the sidelines.

Moreover, at a basic level, the importance of all 50 Senate Democrats being able to cast votes is also critical to moving Build Back Better—something we were all reminded of this week upon learning of Sen. Lujan’s health crisis. The fragility of the power dynamic in the Senate and the continuing threat of outside events disrupting the legislative agenda will require all of us to stay vigilant as 2022 unfolds.

— Jon Traub and Victoria Glover
Tax Policy Group
Deloitte Tax LLP

Deloitte Tax alert looks at new guidance on domestic passthrough entities owning stock in foreign corporations

The Treasury Department and the Internal Revenue Service released final regulations (T.D. 9960) and proposed regulations (REG-118250-20) on January 24 that address a variety of issues relating to the treatment of domestic partnerships and other passthrough entities that own stock in foreign corporations. Among those issues are the determination of subpart F income and section 956 inclusions, the identification of controlling domestic shareholders of a foreign corporation and of the owner of a controlled foreign corporation or qualified electing fund (QEF) for net investment income tax election purposes, and the application of the passive foreign investment company QEF and mark-to-market regimes.

URL: <https://www.federalregister.gov/documents/2022/01/25/2022-00066/guidance-under-section-958-on-determining-stock-ownership>

URL: <https://www.federalregister.gov/documents/2022/01/25/2022-00067/guidance-on-passive-foreign-investment-companies-and-controlled-foreign-corporations-held-by>

The regulations also cover the treatment of S corporations with accumulated earnings and profits attributable to subpart F income and GILTI and the determination and inclusion of related-person insurance income under section 953(c).

Find out more

A new US international tax alert from Deloitte Tax LLP provides an overview of the new regulations.

URL: <https://www2.deloitte.com/content/dam/Deloitte/us/Documents/Tax/dttl-tax-alert-us-28-january-2022.pdf>

— Michael DeHoff
Tax Policy Group
Deloitte Tax LLP

Ways and Means Oversight subcommittee hearing to examine taxpayer problems with IRS

House Ways and Means Oversight Subcommittee Chairman Bill Pascrell, D-N.J., announced this week that his panel will hold a hearing with the National Taxpayer Advocate on February 8 to examine challenges facing taxpayers in dealing with the Internal Revenue Service.

The hearing will take place as the 2021 tax filing season enters its third week and as the agency still struggles to clear a backlog of several million unprocessed tax returns from the 2020 tax year—a situation the Service has attributed to pandemic-related shutdowns and staffing shortages, as well as years of congressionally mandated budget cuts.

National Taxpayer Advocate Erin Collins last month released her annual report to Congress in which she detailed some of the difficulties of the 2020 filing season and cautioned that that she is “deeply concerned” about the possibility of delayed processing of 2021 returns—particularly in the case of taxpayers who file paper returns. Collins also noted in a recent blog post that “taxpayers and practitioners continue to experience frustration over lack of adequate phone service” as they seek answers to questions about advance child tax credit payments, the 2021 recovery rebate credit, unprocessed returns and refund claims, and unresolved 2020 tax return issues.

URL: https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2022/01/ARC21_Full-Report.pdf

URL: <https://www.taxpayeradvocate.irs.gov/news/nta-blog-hello-is-anyone-there-taxpayers-and-practitioners-continue-to-experience-frustration-over-lack-of-adequate-phone-service/>

— Michael DeHoff
Tax Policy Group
Deloitte Tax LLP

This document contains general information only and Deloitte is not, by means of this document, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This document is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte shall not be responsible for any loss sustained by any person who relies on this document.

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited (“DTTL”), its global network of member firms, and their related entities (collectively, the “Deloitte organization”). DTTL (also referred to as “Deloitte Global”) and each of its member firms and related entities are legally separate and independent entities, which cannot obligate or bind each other in respect of third parties. DTTL and each DTTL member firm and related entity is liable only for its own acts and omissions, and not those of each other. DTTL does not provide services to clients. Please see www.deloitte.com/about to learn more.