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Scalise wins House speaker nomination, but drops out after the gavel proves elusive

The House Republican Conference voted by a narrow margin this week to nominate Majority Leader Steve Scalise of Louisiana to serve as the chamber’s next speaker. But for Scalise, winning enough support from his GOP colleagues to secure the majority he needed on the House floor to take the top spot proved to be an even more formidable challenge, and he announced that he was dropping out of the race just one day later.

Done in by math problems

Scalise won the speaker nomination during a closed-door Republican Conference meeting on October 11, defeating his sole declared opponent, House Judiciary Committee Chairman Jim Jordan, R-Ohio, by a vote of 113-99. The speaker is elected by a vote of the entire House, however, so to win the gavel Scalise needed to garner an absolute majority of all members present and voting. Republicans currently hold 221 seats in the chamber, Democrats hold 212, and 2 seats are vacant. With all the chamber's Democrats expected to support of *their* leader, Rep. Hakeem Jeffries of New York, Scalise could afford to lose no more than 4 votes from within the Republican Conference if he hoped to clear the 217-vote threshold required for a majority.

Based on comments by various Republican House members to reporters since the October 11 conference meeting adjourned, it appears that several members—more than enough to sink the nomination—were reluctant to coalesce around Scalise and support his bid for speaker on the House floor. A contingent of more conservative GOP members was intent on voting for Jordan, who is a founding member of the House Freedom Caucus. (Jordan, for his part, had said he would support Scalise and offered to give a nominating speech for Scalise when the time came for a floor vote.) Other Republicans, angered by the way in which a handful of Freedom Caucus members were able to use a "motion to vacate" to force then-Speaker Kevin McCarthy, R-Calif., out of leadership on October 3 after he advanced a stopgap government funding measure that relied on Democratic votes for passage, had declared they intended to support their former leader. (McCarthy stated shortly after losing the speakership that he would not make a bid to reclaim his former job, and even though he appeared to hint earlier this week that he would return to the position if his colleagues demanded it, in the lead-up to the October 11 nomination meeting, he urged conference members not to cast a vote for him.) Still others indicated that they would not support Scalise unless he first committed to meeting an assortment of specific policy demands.

Although there was no official whip count reflecting Scalise's level of support within the conference, various press reports suggested that the holdouts—that is, GOP House members who publicly stated they intended to vote for someone other than Scalise and those who publicly stated that they were not yet committed to supporting him—numbered well into the double digits.

After he secured the nomination, Scalise met individually with holdouts in an attempt to assuage their concerns and he appeared before the entire Republican conference the afternoon of October 12 in a meeting that lasted more than two hours. Despite those efforts, however, he remained short of the level of support he needed to move his nomination to the House floor. (House Republican leaders wanted to ensure that Scalise had locked down the 217 votes he needed to become speaker before they held a floor vote—a strategy they hoped would avoid a repeat of the somewhat chaotic process surrounding Kevin McCarthy's election as speaker in January, which stretched out over four days and 15 ballots.)

Speaker Pro Tempore Patrick McHenry, R-N.C., had alerted members to stand by for a possible floor vote on October 11 and again on October 12 but no votes were called on either day. Scalise was set to meet with the GOP conference on the evening of October 12, presumably for further talks; but with a majority still apparently out of reach, he instead told his colleagues at that meeting that he would no longer seek the speakership.

Next steps uncertain

It was unclear at press time how House Republican leaders intend to manage the process of nominating another candidate for the speaker's post and shepherding him—or her—through a conference that is beset by competing priorities and whose power hinges on an extremely narrow majority. Republicans were expected to hold a candidate forum on the afternoon of October 13 to give speaker-hopefuls an opportunity to make their respective cases to the conference. Rep. Jordan has indicated that he intends to make another run for the speaker's post, though there is concern among some House in the GOP that he, like Scalise, may be incapable of nailing down 217 votes. In addition to Jordan, Rep. Austin Scott of Georgia has declared his own candidacy. Although Scott is considered a heavy underdog in the internal GOP race, his vote total within the conference may indicate the level of difficulty Jordan would have in clinching a majority on the House floor.

Scalise, meanwhile, spoke to reporters shortly after he announced his withdrawal from the race, but was tight-lipped when asked about a potential new field of candidates.

"I am sure there will be a lot of people that look at [running]," he said, "but it's got to be people that aren't doing it for themselves and their own personal interests."

Also unclear is what a prolonged speaker's race will mean for ongoing House operations. Without an elected speaker at the helm, the House has so far not conducted legislative business—a predicament that is growing more urgent by the day as lawmakers face pressures to address priorities such as the looming expiration of the stopgap measure funding the federal government on November 17 and calls from members in both parties to provide emergency support for Israel in its war against Hamas.

Although Patrick McHenry was put in place as speaker pro tempore immediately after the speaker's chair was declared vacant on October 3, his position generally is considered to be ministerial and its powers limited to overseeing the election of a permanent speaker. There are some parliamentary scholars, however, who insist that the speaker pro tempore's authority is far more expansive, which has led some Republicans to suggest that the chamber enhance the powers of the position so that the House can resume operations while the speaker's race continues.

— Michael DeHoff
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Pillar One takes a significant step forward with draft tax treaty, but hurdles remain

The OECD this week took a significant step to advance Pillar One of its ambitious project to update international tax rules, but the plan to reallocate taxing rights still faces an uphill climb, and the Senate's top Republican taxwriter insisted that he is still waiting for Treasury to provide an estimate of the impact of "such sweeping and complex changes to global taxing rights which may have an overwhelmingly disproportionate impact on our companies."

The OECD, which has for several years spearheaded the global tax project involving more than 140 countries, on October 11 released a draft of the multilateral tax treaty it proposes for implementing what is known as Amount A of Pillar One. This element of the agreement would establish a taxing right for market jurisdictions with respect to a defined portion of the residual profits of the largest and most profitable multinational businesses—in short, increasing taxing rights for jurisdictions in which the companies have users and customers. The treaty, known as a multilateral convention (MLC), is not final and is not open for signatures yet. Notes throughout the document identify areas where negotiating countries are still trying to reach agreement.
URL: https://www.oecd.org/tax/beps/multilateral-convention-to-implement-amount-a-of-pillar-one.htm

According to the updated OECD's economic impact assessment published along with the draft treaty, Amount A would have generated $204.6 billion in residual profits in 2021 from 106 multinationals. Low-income countries would experience the greatest revenue gains, the analysis concluded, and, "[b]roadly speaking, Amount A reallocates taxing rights largely from investment hubs towards market jurisdictions (*i.e.*, where [multinationals] have sales or users)." Based on that assessment, investment hubs would have lost between 0.5 percent and 7.9 percent of corporate income tax revenue in 2021 as a result of Amount A and between 0.3 percent to 5.3 percent on average over the 2017-2021 period.
URL: https://www.oecd-ilibrary.org/docserver/7c35a55c-en.pdf

In an October 11 statement responding to the OECD release, Sen. Mike Crapo, R-Idaho, the ranking member of the Senate Finance Committee, said he looks forward to "receiving feedback from our impacted companies on this 800+ page proposal," but added, that "[u]nfortunately—despite repeated requests—Treasury has been unwilling to provide information to determine Pillar One's impact on US companies and revenue." He called on Treasury "to immediately provide that information to Congress."
URL: https://www.finance.senate.gov/ranking-members-news/crapo-congress-still-in-the-dark-on-oecd-pillar-one-global-tax-deal-impact-on-us

Global consensus required

Republican taxwriters have strongly opposed many aspects of the global agreement the Biden administration signed in 2021, but have focused especially on Pillar Two, which would create a global minimum tax. Because Pillar Two does not require global adoption but can be implemented by individual countries, it will have a more immediate impact on US-based companies as jurisdictions plan to begin levying certain new taxes as soon as January 1, 2024.

Pillar One will need broad global consensus to become reality, and in the US it will need sufficient support in the Senate to implement the MLC—support that currently does not seem to exist. And there are other hurdles around the globe: some of the large developing countries at the table, including Brazil, Colombia, and India, are at odds with corporations over the treatment of withholding taxes and the marketing and distribution safe harbor as currently drafted. These challenges, along with other technical disputes, loom over the fate of Pillar

One. OECD tax director Manal Corwin told reporters October 11 that countries are actively trying to resolve their differences on technical issues.

Treasury seeks public comments on MLC

For its part, the US Treasury Department this week announced a request for public comments on the just-released draft MLC.
URL: https://home.treasury.gov/news/press-releases/jy1789

Treasury Assistant Secretary for Tax Policy Lily Batchelder stated in the announcement that the release of the MLC and supporting documents is "a key step forward in the Pillar One negotiations," adding that they "reflect countless hours of discussions, across multiple US administrations, and among hundreds of negotiators." She noted that "Treasury stands behind the negotiations, which have resulted in many difficult compromises by all sides with respect to both the design of the partial reallocation of taxing rights and the elimination of discriminatory digital services taxes and similar measures"; but she added that "Pillar One represents a uniquely significant reform to the international tax system" and [b]ecause of the breadth and complexity of the changes proposed, we view public input as critical to our process—to ensure transparency, to facilitate the resolution of several remaining open issues, and to hear whether the proposed framework would be workable for US taxpayers and other stakeholders."

Written comments are due December 11, 2023, and must be submitted electronically to: OTP_Pillar1MLC@treasury.gov.
URL: mailto:OTP_Pillar1MLC@treasury.gov

The future of DSTs

A key motivation for the US originally engaging in the OECD project was the promise of new global rules that would end the proliferation of digital services taxes (DSTs) largely impacting US-based tech companies. With taxing jurisdictions from around the globe at the negotiating table and willing to discuss base erosion and profit shifting, reallocation of taxing rights, and a global minimum tax, the US was able to secure a pause on new DSTs through 2023 (or until a new Pillar One multilateral convention came into force, if that occurred sooner).

With the work on Pillar One behind schedule, 138 of the 143 negotiating countries released a statement in July agreeing to extend the current moratorium on DSTs and other similar relevant taxes through 2024, with one important condition: at least 30 jurisdictions accounting for at least 60 percent of the ultimate parent entities of in-scope businesses must sign the multilateral convention before the end of 2023. This condition would appear to indicate that the negotiators expect the US to sign the MLC, given that more than 40 percent of in-scope companies reportedly are headquartered in the US. While the prospect of Congress agreeing to implementation of Pillar One in the foreseeable future is dim, the Biden administration could still sign the MLC and then later push for legislative approval.

The July statement also provided for the possibility of a further one-year extension of the moratorium, through the end of 2025, if member countries agree that "sufficient progress has been made by [the end of 2024] towards the entry into force of the MLC."

In his statement this week, the Finance Committee's Mike Crapo said, "While I oppose discriminatory [DSTs] targeting US companies, I also want to ensure that the OECD cure is not worse than the DST disease for US businesses and workers."

This week's draft MLC includes in an appendix a list of nine existing measures that would be subject to removal upon implementation of the treaty, including a DST in France that sparked threats of retaliatory taxes and tariffs by the US in 2019.

Oh, Canada

Among the five countries that did not agree to the July statement extending the DST moratorium was Canada, which has insisted it will move ahead with its plans to impose a DST beginning January 1, 2024, because there is no "firm and binding multilateral timeline to implement Pillar One."

Reiterating points recently made by House taxwriters, Senate Finance Committee Chair Ron Wyden, D-Ore., and ranking member Crapo this week sent a letter to US Trade Representative (USTR) Katherine Tai insisting that she "make clear that [the USTR's] office will immediately respond using available trade tools upon Canada's enactment of any DST." The senators added that USTR would have their "full support" in adopting retaliatory trade measures.
URL: https://www.finance.senate.gov/imo/media/doc/20231010wydencrapolettertoustroncanadadst.pdf

"This is not a matter that warrants extensive new analysis," Wyden and Crapo wrote. "The details and content of this tax are already well known and established. USTR has exhaustively examined nearly identical measures and has convincingly demonstrated why they are discriminatory against the United States." (For prior coverage of comments from House Ways and Means Committee members on Canada's DST, see *Tax News & Views*, Vol. 24, No. 31, Sep. 22, 2023.)
URL: https://dhub.deloitte.com/Newsletters/Tax/2023/TNV/230922_4.html

Tai, US ambassador to Canada David Cohen, and Treasury official Michael Plowgian have all publicly called on Canada to maintain the current DST moratorium while OECD work continues, and Treasury Secretary Janet Yellen has reportedly engaged directly with her Canadian counterpart on the issue.

Canada's DST is a 3 percent tax on the revenue large businesses earn from online marketplaces, social media platforms, the sale and licensing of user data, and online ads. Unless Canada backs down before January 1, 2024—which it currently indicates it will not do—it will begin collecting the tax retroactive to January 1, 2022.

— Storme Sixeas
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Tax gap estimate climbs to $688 billion, IRS says

The gross federal tax gap—the difference between the amount of tax legally owed to the government and the amount paid and collected on a timely basis—reached an estimated $688 billion in tax year 2021, according to a new report released by the Internal Revenue Service on October 12.
URL: https://www.irs.gov/pub/irs-pdf/p5869.pdf

The projections, which cover tax years 2020 and 2021, represent an increase of more than $192 billion from the IRS's prior estimates for tax years 2014-2016 and $138 billion from the revised projections for tax years 2017-2019, the agency said.

Elements of noncompliance

Across the three main components of the tax gap, the report shows that the gross revenue shortfall breaks down this way:

- Nonfiling, that is, tax not paid on time by those who do not file on time, amounted to $77 billion in tax year 2021, up from $41 billion in tax years 2017-2019;
- Underreporting, which reflects tax understated on timely filed returns, accounted for $542 billion in foregone collections in tax year 2021, up from $445 billion in tax years 2017-2019; and
- Underpayment, or tax that was reported on time but not paid on time, rose to $68 billion in tax year 2021, from $64 billion in tax years 2017-2019.

The net annual tax gap for tax year 2021, reflecting late payments plus amounts recouped through IRS enforcement efforts, is projected to reach $625 billion, the IRS said.

Compliance rates

The report notes that the voluntary compliance rates for tax year 2020 and 2021 tax gap held steady at roughly 85 percent.

After IRS compliance efforts are factored in, the projected share of taxes eventually paid is 86.3 percent for tax year 2021, down slightly from the 87 percent for tax years 2014-2016; however, the report attributes the decline to changes in the types of income and how that income is reported to the IRS rather than changes in taxpayer behavior.

Caveats

The IRS cautions that there are several reasons why the new estimates likely do not reflect the full extent of taxpayer noncompliance, including:

- The lack of available data to completely measure noncompliance levels in areas of the tax system such as offshore activities, digital assets and cryptocurrency, corporate income tax, income from flowthrough entities, and illegal activities;
- The lack of a reliable method for measuring taxpayer behavior related to claims for pandemic tax credits enacted on an emergency basis in 2020 and 2021;
- The level of time and training required for the IRS to develop expertise related to digital assets and other emerging issues and to complete examinations that can be used to capture the extent of that noncompliance.

The report states that "the IRS continues to actively work on new methods for estimating and projecting the tax gap to better reflect changes in taxpayer behavior as they emerge."

The report also notes that the collections shortfall associated with illegal activities is outside the scope of tax gap estimation because the government's objective is to eliminate those activities, which would eliminate any associated tax.

IRS funding a hot-button issue on Capitol Hill

Release of the latest tax gap projections comes as partisan divisions persist in Congress over the 10-year mandatory funding allocated to the IRS under the Inflation Reduction Act (P.L. 117-169) to beef up its enforcement efforts as well as modernize its information technology and improve its customer service. As enacted, the Inflation Reduction Act provided the agency with $80 billion in new funding, although roughly $20 billion of that amount will be rescinded as part of a "handshake" deal between President Biden and then-Speaker Kevin McCarthy, R-Calif., when they negotiated the Fiscal Responsibility Act (P.L. 118-5), the debt limit deal that was signed into law this past June.
URL: https://www.congress.gov/117/plaws/publ169/PLAW-117publ169.pdf
URL: https://www.congress.gov/118/plaws/publ5/PLAW-118publ5.pdf

Democrats generally have argued that the Inflation Reduction Act funds will give the IRS the resources it needs to audit the increasingly complex returns of large corporations and partnerships and ultrawealthy individuals that often have opaque sources of income and engage in highly sophisticated tax transactions. The contention among some factions of GOP lawmakers, however, is that the IRS intends to use the funds to hire an "army" of new revenue agents focused on audits of small businesses and middle-class individuals.

IRS Commissioner Daniel Werfel commented in an October 12 news release that the latest estimates "underscore the importance of increased IRS compliance efforts on key areas." The Inflation Reduction Act funding, he said, is enabling the agency to "add focus and resources to areas of compliance concern, including high-income and high-wealth individuals, partnerships, and corporations," which, in turn, will "[add] more fairness to the tax system" and "[protect] those who pay their taxes. . . ."

— Michael DeHoff
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CBO reports $1.7 trillion budget deficit for FY2023 on account of falling revenues

The nonpartisan Congressional Budget Office (CBO) this week estimated that the budget deficit for the federal fiscal year that ended on September 30, 2023, totaled $1.7 trillion—about $300 billion more than the prior fiscal year—a result the agency attributed to the net effect of both falling revenues and, to a lesser extent, lower outlays on federal spending programs.

Big dip in revenues

CBO's report—published October 10 in the form of a "monthly budget review" for September 2023—projects that federal revenues fell by $455 billion (or 9 percent) over the course of fiscal 2023 as compared to the prior fiscal year. The biggest driver of this drop relates to nonwithheld payments of income and payroll taxes (down $296 billion), which CBO states could be attributable to lower capital gains receipts as well as the fact that the Internal Revenue Service postponed the filing and payment deadlines for certain taxpayers affected by natural disasters until mid-October (thus pushing those receipts into fiscal year 2024).
URL: https://www.cbo.gov/system/files/2023-10/59544.pdf

Receipts from other sources—such as remittances from the Federal Reserve, customs duties, excise taxes, and miscellaneous fees and fines—also fell by a considerable $124 billion compared to last year. Most of this drop ($107 billion), however, relates to Fed remittances, which the CBO notes stem from higher short-term interest rates, which have served to eliminate net interest income at many Federal Reserve banks.

As for corporate income taxes, CBO projects a drop of $5 billion from fiscal year 2022, an outcome the agency predicts could also be linked to disaster-related extensions of payment deadlines.

It is important to note that the figures published by CBO this week are somewhat preliminary and the official fiscal metrics for the just-concluded fiscal year will be released in the near future, likely when the agency publishes its next 10-year economic and budget outlook—the so-called budget "baseline" that serves as the benchmark against which Congress measures the fiscal impact of tax and spending proposals on a prospective basis.

"The reasons for the difference [in revenues] will be better understood as additional information becomes available," CBO states in this week's report.

Partial offset due to drop in spending: The report also estimates that federal spending, on net, fell by $141 billion (or 2 percent) in fiscal year 2023 relative to the prior fiscal year. A sizable part of that drop, however—

$54 billion—was attributable to a simple timing shift: October 1 fell on a Saturday in 2022, which meant that outlays that otherwise would have been made in fiscal year 2023 were pulled into fiscal year 2022 instead.

Another large component of the spending drop ($120 billion) relates to refundable tax credits (which are accounted for as outlays), specifically the expiration of the expanded child tax credit Democrats enacted for tax year 2021 in the American Rescue Plan (P.L. 117-2). Advance payments of the expanded credit were made between July and December of 2021, and thus spanned fiscal years 2021 and 2022.
URL: https://www.congress.gov/117/plaws/publ2/PLAW-117publ2.pdf

Fodder for both sides

This week's CBO report will surely become fodder for both Democrats and Republicans in the coming weeks as lawmakers again face a potential partial government shutdown on November 17. Congress narrowly averted a shutdown on September 30 when then-House Speaker Kevin McCarthy, R-Calif., bucked many conservative members of his party and moved a so-called "clean" continuing resolution that received broad support from both Democrats and moderate Republicans and served to keep the government's doors open for seven weeks into current fiscal year 2024, but at the same time contributed to his ouster as speaker. (For prior coverage, see *Tax News & Views*, Vol. 24, No. 33, Oct. 6, 2023; see related coverage in this issue for the current dynamics surrounding the House GOP's selection of a new speaker.)
URL: https://dhub.deloitte.com/Newsletters/Tax/2023/TNV/231006_1.html

Over the longer term, large and growing budget deficits—such as the one for fiscal 2023 highlighted by the CBO this week—are sure to play an enormous role in upcoming debates over fiscal policy, including the pending sunset of much of the Tax Cuts and Jobs Act of 2017 (P.L. 115-97) and the looming insolvencies of the Social Security and Medicare trust funds, all of which are on the horizon at the same time that budget forecasters have been ratcheting up their estimates of the government's debt service costs on account of higher interest rates.
URL: https://www.congress.gov/115/plaws/publ97/PLAW-115publ97.pdf

In its most recent 10-year budget outlook published in May, the agency predicted that budget deficits will climb consistently until they reach almost $2.9 trillion in fiscal year 2033 and that, over the next decade, cumulative deficits would top $20 trillion.
URL: https://www.cbo.gov/publication/59096

But, at least for now, we can expect that lawmakers will continue to talk past one another when it comes to their views of the root of the fiscal mismatch and what should be done to address it, with Democrats generally arguing it is problem driven primarily by insufficient revenues, especially in light of structural factors like an aging population that is driving up the costs of broadly popular programs like Social Security and Medicare, and Republicans laying the blame mainly on the spending side of the ledger.

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Deloitte Tax looks at SEC's adoption of 'T+1' settlement cycle and its impact on stock based compensation

The Securities and Exchange Commission (SEC) has adopted a rule change to shorten the standard settlement cycle for most broker dealer securities transactions from two business days after the trade date (T+2) to one (T+1). The effective date for the final rule is May 28, 2024.

That rule change will put increasing pressure on employers to ensure broker dealers are equipped with the data points to settle certain employee equity award transactions. Equity award settlement involves coordination among multiple stakeholders—broker, payroll, tax and transfer agent, to name a few—and in a narrower window of time. It also suggests that employers should assess and determine whether their equity compensation programs are operating in a manner that not only allows the employer to meet its tax compliance obligations but also meet employee expectations.

Find out more

A new publication from Deloitte Tax LLP's Global Employer Services group discusses the impact of the SEC's new rule on equity compensation plans and what companies can do to prepare for the coming change.
URL: https://dhub.deloitte.com/Newsletters/Tax/2023/TNV/231013_5_suppA.pdf

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