Washington National
Tax Services (WNTS)

2025 Tax Policy Outlook:

A year for action

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Overview

A key challenge for business leaders this year will be to engage with policymakers and to build public support for tax and trade policies that promote economic growth, business investment, and job creation.

The start of the new 119th Congress and the inauguration of Donald J. Trump as president marks the beginning of a year for action on a significant "must-pass" tax bill. The incoming Trump administration and a Republican-controlled Congress are facing a December 31, 2025 deadline to extend key 2017 Tax Cuts and Jobs Act (TCJA) individual, business, and international provisions set to expire or change at the end of this year. While some key decisions on timing and process could change, Republicans are unified in holding that failure to enact a tax bill this year is not an option. A lack of action would result in across-the-board tax increases on virtually every individual taxpayer and automatic increases in some business taxes.

At the same time, the global tax policy landscape continues to undergo significant transformation due to pressures from tax competition, globalization, and digitalization. These factors are intensified by governments' need to increase revenue to address national deficits, maintain social services, increase defense spending, and advance sustainable development goals, especially in the Global South. Just as economic populism is playing a role in US policy debates, the global call for multinational corporations (MNCs) to pay additional taxes and demands for reallocating taxing rights to market jurisdictions remain unsatisfied.

The November 2024 elections marked a pivotal moment for US trade policy. President Donald Trump's return to the White House signals a potentially transformative shift in global trade relations. During the campaign as well as the period following the election, Trump proposed substantial tariffs aimed at reshaping US trade relations, especially with respect to China, and encouraging domestic manufacturing.

A key challenge for business leaders this year will be to engage with policymakers and to build public support for tax and trade policies that promote economic growth, business investment, and job creation. If the business community fails to engage, the terms of the debate over the tax and trade policy choices ahead will be set without the facts and insights that the business community uniquely provides on the impact of policy choices on the US economy, business, and individuals.

A new start for a returning president and a Republican-controlled Congress

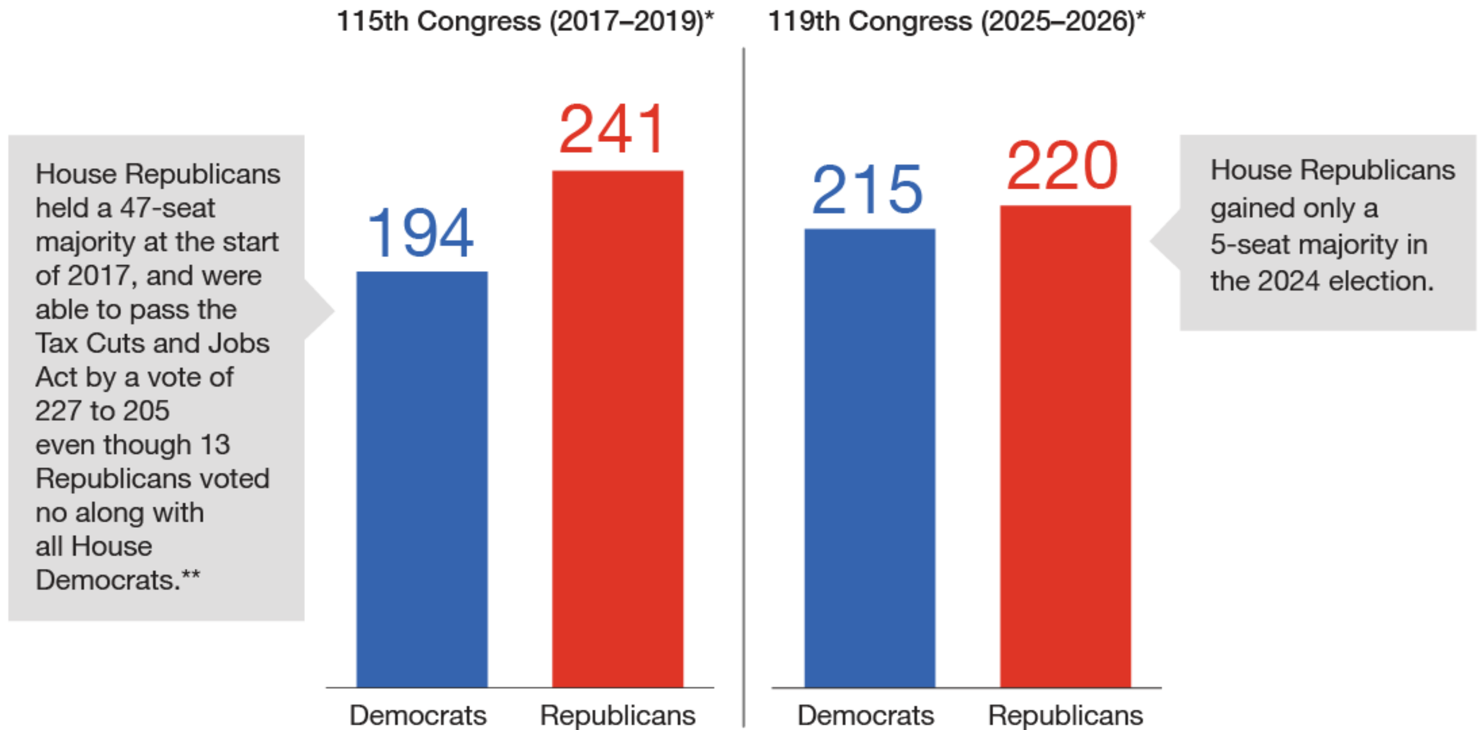
Donald J. Trump has become only the second president in US history to serve two non-consecutive terms. The new 119th Congress has the potential to act on the policy goals advanced by the president and Republicans who will control the House and Senate, but the path forward could be challenging. On January 5, President Trump called for Congress to "work on one powerful bill" that would focus on border security, increased US energy production, and renewing the TCJA tax cuts as well as enacting key campaign tax proposals. The next day he followed that up by indicating openness to a two-bill strategy, emphasizing the priority is to "get something passed as quickly as possible."

While House Republicans won a 220 to 215 majority in last November's elections, returning Speaker Mike Johnson (R-LA) is leading a reduced 219 to 215 majority at the start of the new Congress, with one vacant seat due to re-elected Rep. Matt Gaetz (R-FL) not taking his seat. A presidential cabinet nomination of Rep. Elise Stefanik (R-NY) and White House staff appointment of Rep. Michael Waltz (R-FL) will further reduce the House Republican majority to 217 until special elections are held to fill the three vacancies. Speaker Johnson has stated that Congress should work to complete a reconciliation bill addressing President Trump's priorities by the end of May.

Observation: By contrast with the current narrow House Republican majority, House Republicans held a 47-seat majority in 2017, allowing the TCJA to pass by a vote of 227 to 205 even though 13 House Republicans opposed the 2017 bill, as shown in Figure 1.

New Senate Majority Leader John Thune (R-SD) will have to keep his narrow 53 to 47 seat majority unified on the many key votes that will need to be taken this year. In addition, the Senate early this year will be responsible for confirming the many individuals who have been nominated to serve in the Trump administration. Majority Leader Thune and others had supported a two-bill reconciliation strategy that would have sought to enact a border security bill first and then address the TCJA tax provisions and other issues by early summer in a second bill.

Figure 1: New House Republican majority is razor thin compared to 2017 when TCJA was enacted



*Party division totals are based on election day results.
** TCJA House total vote count does not equal 435 due to absent members not voting.

Source: US House

The year begins with many open questions:

- Will Republicans in Congress with their narrow majorities, especially in the House of Representatives, be able to reach near-unanimous agreement to enact "one powerful bill" using reconciliation procedures with only Republican votes or will they revert to the two-bill strategy that emerged at the end of 2024?
- How will a significantly worsened fiscal outlook for the federal government affect tax and trade policy decisions that could add to the historic levels of US national debt?
- How will a more populist Republican administration and Congress balance a desire to extend and expand tax cuts for individual Americans with the need to also preserve and expand pro-growth business tax policies?
- While an increase in the 21% US corporate income tax rate appears unlikely, will fiscal and political pressures lead Congress to adopt some revenue-raising offsets for a tax bill that could degrade the domestic investment environment?
- How will the Trump administration and Congress respond to concerns about the potential for US companies to pay a higher overall tax rate to other governments under the new Pillar Two global minimum tax regime?

- How will a more activist US trade policy agenda built around the prospect of higher tariffs affect supply chains and the potential for retaliatory responses from key foreign trading partners?
- What is the outlook for maintaining or increasing incentives for US domestic production in key sectors, including technology and energy?
- What actions will state governments take to adjust to changing federal policies?
- How will ongoing inflation pressures, higher interest rates, and a strong US job market affect policy decisions and the outlook for economic growth?

In addition to these many questions about the outlook for US tax and trade policy, the Trump administration will have to contend with the January 1 reinstatement of statutory US debt limit and avoid a government shutdown after March 14, when a temporary 2025 fiscal year (FY) funding measure is set to expire.

While the incoming Trump administration's Treasury Department can use "extraordinary measures" to postpone the need for an increase in the statutory debt limit until later in the year, the rapid growth of the US federal debt to more than $36 trillion — up from $20 trillion in 2017 when Trump first entered the White House — could affect key decisions on a 2025 tax bill.

During action last December on a temporary FY 2025 funding measure, President Trump called for suspending the debt limit for an additional two years. The House rejected a temporary funding proposal that would have included a suspension of the debt limit through January 29, 2027, by a vote of 174 to 235, with 38 Republicans and 197 Democrats voting no. President Trump also questioned the wisdom of the debt limit and argued it should be eliminated.

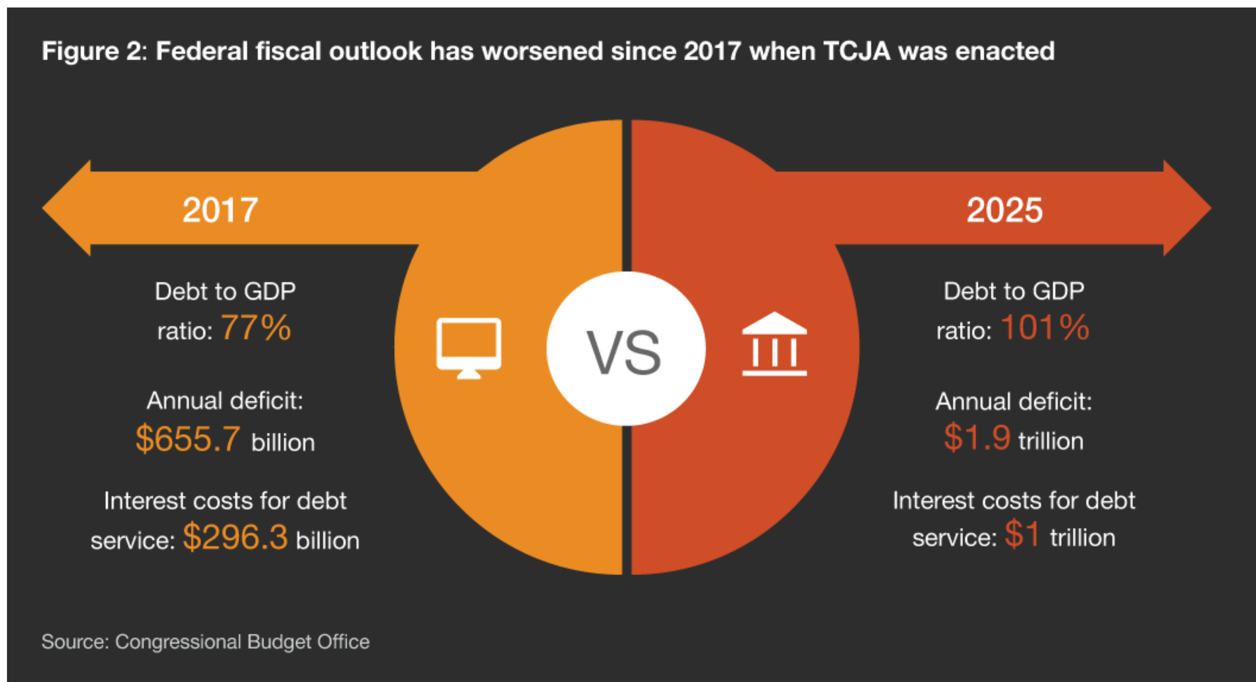
To secure passage of another temporary measure funding the government through March 14, House Speaker Johnson was reported to have proposed that a $1.5 trillion debt limit increase would be paired with proposals to reduce spending by $2.5 trillion.

Observation: The difficulty of House Republicans securing the votes to pass a temporary funding bill last December appears to have been a factor in President Trump endorsing a one-bill reconciliation effort that would address border security, energy production, and tax proposals as well as mandatory spending cuts. Legislation addressing the debt limit generally has been expected to require the votes of House and Senate Democrats, since many Congressional Republicans have regularly voted against legislation to increase or suspend the debt limit. It remains to be seen whether a debt limit increase will be addressed as part of a reconciliation bill since this could complicate prospects for Republicans to secure the votes needed to pass a bill that Democrats would likely oppose.

Legislation to approve government funding for the remainder of FY 2025 also will require the support of Senate Democrats, since Republicans hold 53 seats in the Senate and at least 60 votes generally are required for passage of appropriations bills.

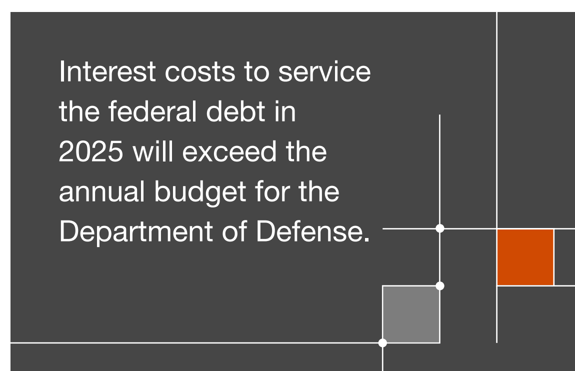
Observation: Bond rating agencies have downgraded US Treasury bonds during previous periods of uncertainty about the federal government's political capacity to avoid a default on the nation's publicly held debt obligations. Under the terms of the "Fiscal Responsibility Act of 2023" (FRA), failure to reach an agreement in March on a funding bill for the remainder of FY 2025 could result in an across-the-board reduction in defense and nondefense spending if another temporary funding bill were to continue into April. The FRA was negotiated by President Biden and former House Speaker Kevin McCarthy (R-CA) as part of the most recent action to temporarily suspend the statutory debt limit. Rep. McCarthy was removed as speaker by the House later that year.

Figure 2: Federal fiscal outlook has worsened since 2017 when TCJA was enacted



Source: Congressional Budget Office

The new Trump administration and Congress will need to address a host of other domestic and foreign policy issues, including border security and possible changes to US immigration laws, the ongoing conflict in Ukraine since Russia's 2022 invasion, conflicts in the Middle East, and geopolitical competition with China. Action also will be required this year to reauthorize US farm and nutrition programs and other expiring federal programs.



It is unclear at this early stage what legislative or executive actions may be taken in response to efforts by a presidential advisory commission, the "Department of Government Efficiency," to reduce federal spending, increase government efficiency, and reduce regulatory burdens.

Preparing for a 2025 tax bill

Republican control of the White House and Congress will allow for the use of budget reconciliation procedures to enact tax legislation in 2025 with only Republican votes, as was the case in 2017 when the TCJA was enacted. While reconciliation procedures are subject to certain procedural limitations, they do allow for Senate passage of legislation by a simple majority vote (including the tie-breaking vote of the Vice President, if needed), instead of the 60-vote majority generally required in the Senate to approve legislation.

Senate debate is also subject to specific time limits of 50 hours on the budget resolution, 20 hours on each reconciliation bill, and 10 hours on the conference report. Motions to instruct conferees also provide debate time. In addition, restrictive rules of germaneness protect a bill that is reported by Senate committees.

Observation: Federal debt concerns and the narrow margins of the House and Senate Republican majorities could complicate the ability of Republican Congressional leaders to extend TCJA tax provisions and enact all of President Trump's campaign proposals.

At this writing, the incoming Trump administration and Republican leaders in Congress appear to be leaning towards focusing on one large reconciliation bill package that would address tax issues as well as border security, energy production, and mandatory spending cuts during the 2025 calendar year.

To advance this reconciliation bill strategy, the House and Senate will need to approve a budget resolution providing reconciliation instructions for the committees that would be charged with drafting legislation. The budget resolution and the subsequent reconciliation bill would need to secure the support of nearly all House and Senate Republicans in a narrowly divided Congress.

It is anticipated by House Republicans that action on this reconciliation bill might be completed before the end of May, with action on a budget resolution possible as early as February. Technically, an FY 2025 reconciliation bill would have to be completed before September 30, 2025, when the federal government's FY 2025 will end. If efforts are made to include an increase in the statutory debt limit as part of a reconciliation bill, the deadline could be when Treasury announces that the X-date is approaching, after which the federal government would be at risk of defaulting on publicly held debt repayments. Currently, Treasury is not expected to reach this X-date until midsummer.

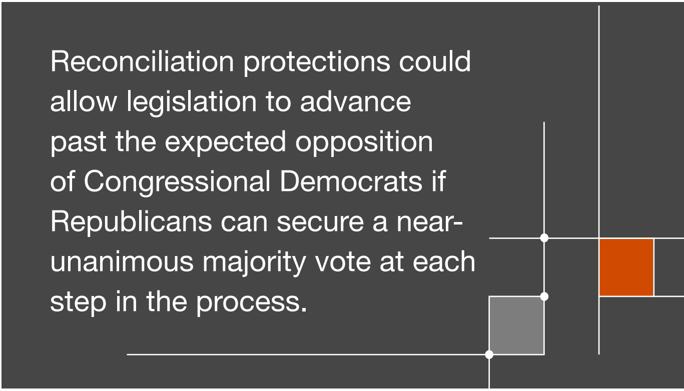
Observation: Reaching an agreement on how to address expiring TCJA tax provisions, President Trump's campaign tax proposals, and other issues under a budget resolution that balances fiscal concerns and differing priorities among various Republican members in Congress could delay action on a reconciliation bill.

In support of a one-bill reconciliation approach, House Speaker Johnson has noted past challenges in attempting to complete two reconciliation bills in the first year of a new administration. Two reconciliation bills were attempted in 2017 during President Trump's first year in office. The first reconciliation bill that proposed to "repeal and replace" the Affordable Care Act failed in the Senate, but the second, the TCJA, was enacted in late December. The Biden administration also attempted to complete two reconciliation bills in 2021. The first, the American Rescue Plan providing additional pandemic relief, was enacted in March, but the second, a House-passed Build Back Better bill, which in the Senate became the Inflation Reduction Act, was not enacted until August 2022.

The current Congress could still consider a second reconciliation bill later this year under an FY 2026 budget resolution if necessary.

Under the earlier two-bill reconciliation approach, it was contemplated that a first reconciliation bill would primarily address border security and certain related issues that could be considered under an FY 2025 budget resolution in several weeks early this year. After hopefully securing an early policy win on border security, a second reconciliation bill to address expiring TCJA tax provisions, Trump campaign tax proposals, and other proposals that might include reductions in mandatory spending programs was to be considered under an FY 2026 budget resolution, with the goal of completing this legislation by early summer. Under Congressional budget rules, this second reconciliation bill could be enacted as late as September 30, 2026, but the practical deadline would more likely be December 31, 2025, when key TJCA tax provisions are set to expire.

Observation: Only if efforts to enact a reconciliation bill have failed would President Trump and Congressional Republicans be expected to negotiate a compromise bill with Congressional Democrats to extend expiring TCJA tax provisions. In such a situation, Democratic votes might be needed to avert an across-the-board tax increase for individuals and businesses after December 31, 2025.



Global tax policy changes with or without the United States

Countries continue to implement the second part of the two-pillar approach of the Organization for Economic Co-operation and Development (OECD)/G20 Inclusive Framework on Base Erosion and Profit Shifting. Pillar Two aims to establish a coordinated global minimum corporate tax rate and has been adopted by many developed economies, particularly in Europe.

While the outgoing Biden administration played an instrumental role in urging adoption of a global minimum tax by the OECD and G20 nations, implementation of the Pillar Two minimum tax provisions in the United States appears highly doubtful. The Congress, however, is expected to address scheduled changes to TCJA international tax provisions.

Under the TCJA, key international tax provisions are scheduled to change after 2025. The global intangible low-taxed income (GILTI) regime and the base erosion and anti-abuse tax (BEAT) are scheduled to become more restrictive. The deduction for foreign derived intangible income (FDII) is scheduled to be reduced and look-through treatment for certain controlled foreign corporation (CFC) income is set to expire.

Observation: Regardless what the United States does (or does not do) in 2025, US MNCs with operations in jurisdictions that have adopted Pillar Two-inspired minimum taxes will be subject to their requirements, including considerable reporting obligations.

Key Republican lawmakers, including House Ways and Committee Chairman Jason Smith (R-MO) and new Senate Finance Committee Chairman Mike Crapo (R-ID), have objected to the projected detrimental impact of Pillar Two on the US fisc. The Undertaxed Profits Rule (UTPR) has become a focal point for critics of Pillar Two because of its potential to undermine a country's sovereignty over its tax policy (and possible violations of international agreements, including bilateral tax treaties). In the United States, those critics have threatened to take a range of actions, from retaliatory taxes or tariffs to reducing funding to the OECD.

Observation: The Trump administration and Congressional Republicans are expected to oppose the OECD's two-pillar deal and may consider retaliatory measures against companies based in jurisdictions enforcing such taxes. Republican members in both chambers have been highly critical of the Biden administration's handling of the OECD negotiations and have expressed concerns that these proposals undermine the US tax base and put the United States at a competitive disadvantage relative to other countries.

While many countries have moved forward with implementing Pillar Two, consensus on Pillar One, which aims to reallocate a portion of MNCs' profits to market countries, continues to be elusive. This has led to increased skepticism about its ultimate adoption. According to the OECD, the goal is to have a Pillar One Multilateral Convention (MLC) ratified by a critical mass of countries and enter into force in 2025. The extension of the moratorium on new digital services taxes (DSTs) was conditional on the MLC being signed in 2024, but this did not happen.

Observation: A major justification for the negotiations leading to Amount A of Pillar One was the possibility of eliminating DSTs. With the growing realization that Amount A will not be implemented, many countries, particularly Global South countries with lower per-capita income located primarily in Africa, Asia, Latin America, the Caribbean, and Oceania, are discussing policy options that include enacting and potentially harmonizing DSTs and other similar measures. The European Union (EU) also has signaled support for a European solution for digital taxation if it is not possible to secure support from the United States on Pillar One Canada in 2024 moved forward with its DST.

Meanwhile, the OECD's long-recognized authority over multilateral international tax reform process has faced challenges from individual countries taking independent unilateral action and from the United Nations (UN), which has asserted a greater role in global tax policy. Many of the UN's members from the Global South have expressed dissatisfaction with the pace of the negotiations under the OECD/G20 Inclusive Framework as well as the disparate impact of the various rules on developing countries.

Issues to consider:

- While Pillar One adoption remains doubtful, Pillar Two is being widely implemented by most of the United States' largest trade partners. Companies should prepare for further guidance on the global minimum tax rules and potential changes to the UTPR due to expected pushback from the United States.
- The trend toward unilateral DSTs likely will increase without progress on Pillar One.
- The role of the UN in global tax policy is likely to grow, introducing further uncertainties for businesses.

Overall, businesses must navigate a complex and evolving international tax environment characterized by political tensions, regulatory uncertainty, and potential unilateral actions by countries. Businesses are encouraged to engage proactively with policymakers as the international tax framework evolves, given the heightened political pressure.

Trade policy takes center stage

The incoming Trump administration has laid out an activist trade policy agenda built around proposals for substantial increases in tariffs that is intended to reshape US trade relations and encourage domestic manufacturing. The trade policy landscape under President Trump could involve substantial disruption and uncertainty. It is currently unclear whether tariff revenues might be used to offset part of the cost of a 2025 tax bill.

Since the November elections, President Trump has focused his proposed tariff actions on key trading partners including China, Mexico, and Canada, suggesting trade policy actions affecting imports from these countries could be implemented as early as the first day of his new term.

Observation: President Trump could be utilizing the threat of tariffs as a negotiation tool to encourage trading partners to take stronger measures in the geopolitical policy arena, including border security and exports of illicit substances. While a successful negotiation for a standstill of tariffs could ultimately yield something less destabilizing to global trade, it remains unclear whether the President's actions will remain negotiation tactics or transform into a springboard to upend existing trade agreements and increase tariffs. Therefore, companies need to be proactive and model the potential impact of a range of possible outcomes.

The Trump administration may rely on numerous statutes to impose or increase tariffs unilaterally. These statutes currently provide the president with substantial ability to impose a wide range of tariffs. However, broader measures may require Congressional approval, particularly those tied to revenue generation for tax reform.

Congress over several decades has delegated significant trade authority to the president in several statutes, including Section 232 of the Trade Expansion Act of 1962 and Section 301 of the Trade Act of 1974, as shown in Appendix C.

Proposed tariff rates and implementation pathways

The Trump administration has outlined an aggressive tariff agenda with rates that diverge significantly from current trade norms. Key proposals include:

- An **additional 10% tariff** or a flat **60% tariff** on all Chinese-origin products to reinforce the administration's focus on strategic competition.
- Tariffs ranging from **100% to 200%** on vehicles imported from Mexico, significantly impacting the automotive sector.
- A **25% tariff** on all imports from Mexico and Canada, indicating a recalibration of the United States-Mexico-Canada Agreement (USMCA).
- A **10% to 20% tariff** on all rest-of-world (ROW) imports (not already covered above) to incentivize domestic production.

Following his election, President Trump in late 2024 stated that he would require countries in the BRICS group — a coalition of emerging economies supported by China and Russia — to pledge not to create new currencies or back currencies other than the US dollar, or face 100% tariffs during his administration.

Observation: The first Trump administration imposed and threatened to escalate existing tariffs, but following his re-election four years later, there is uncertainty about the scope of future tariff policies, suggesting a potential shift from past approaches. While it is uncertain at what rates and by what methods the incoming administration will impose new tariff measures, it is likely there will be new tariff increases in 2025.

Figure 3: Trump administration tariff proposals

Trump Administration				
China	Canada	Mexico	Rest of the world	Total
Chinese origin products at additional 10% or a flat 60%	Products imported from Canada at 25%	Products imported from Mexico at 25%	RoW origin products at 10% to 20%	Total prospective Trump tariff impact for a company would equal sum of potential tariff increases for all countries

Note: Calculations assume that the tariffs are on top of any existing free trade agreement benefits given this is unclear from President-elect Trump's administration

Source: Trump for President 2024

Additionally, there are industries and products captured in these proposals that were not subject to punitive tariffs under previous administrations. Even Chinese goods that were previously exempt from punitive tariffs would be impacted by the new Trump tariff proposals, and importers of all goods need to consider the potential impact on a go-forward basis.

The United States is expected to continue the use of additional measures to address concerns about geopolitical competition with China. Various executive orders have been issued to prohibit or restrict the export of certain technologies and products to China. Legislative proposals also were proposed in the last Congress to expand current administrative restrictions on certain US investments in China.

Economic and budget outlook

The growth rate for real gross domestic product (GDP) increased to 3.1% in the third quarter of 2024 from 3.0% in the second quarter of 2024. Growth is expected to slow in 2025. The January Blue Chip Economic Indicators forecast growth of 2.0% for 2025, compared with the average growth rate of 2.7% for the last 50 years.

Labor market conditions softened somewhat in the fourth quarter of 2024. After weakness in October due to strike activity, the job market recovered in November and December, with the unemployment rate having increased from 3.7% in January, but remaining low at 4.1% in December. Federal Reserve economists expect the unemployment rate to rise to 4.3% by the end of 2025. Payroll employment increased by 2.2 million in 2024 (an average monthly gain of 186,000, down from 3.3 million jobs in 2023 (251,000 on average). Job openings continue to exceed job seekers, but labor demand has moderated, thereby easing pressures on wages.

Though interest rates remain somewhat elevated, financial conditions are providing only modest headwinds to economic activity that are expected to reduce GDP growth by less than 0.3 percentage points over the next year. The Federal Reserve Board reduced its target range for interest rates by 25 basis points in December, citing progress toward its 2% inflation objective. It remains committed to supporting maximum employment and returning inflation to its target level of 2%. Monetary policymakers and financial markets expect rates to continue to decline in 2025, though somewhat more slowly than previously anticipated, with only another 50-basis-point reduction by the end of the year.

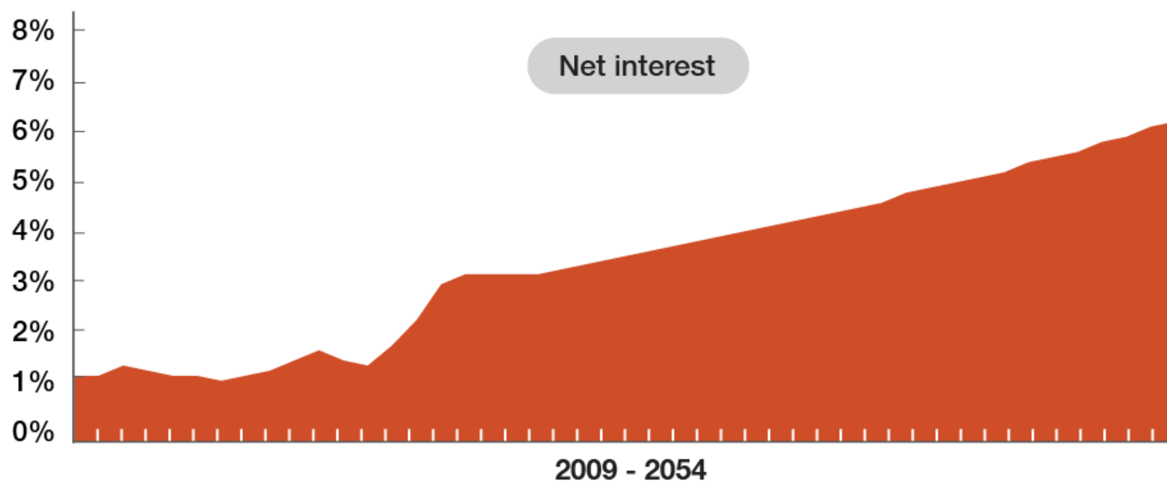
The International Monetary Fund (IMF) has issued revised global economic forecasts that project world GDP growth of 3.2% in 2025. The forecast for 2025 is 0.1 percentage points lower than its July estimate for 2025, reflecting upward revisions of growth in the United States and downward revisions in other advanced economies. Inflation is expected to continue its downward trajectory across the world, although the pace of disinflation is projected to be faster in advanced economies than emerging and developing economies. Achieving inflation targets is expected to take until the end of 2025 in most instances.

The IMF identifies a number of downside risks, including delayed, but higher-than-anticipated, negative economic effects from monetary policy tightening; persistently high near-term inflation expectations that may change the path of monetary policy; high sovereign debt spreads that may cause fiscal consolidation in certain countries; deep contraction in the Chinese real estate market; commodity price shocks arising from conflicts; and protectionist trade policies, including the prospect of rising tariffs.

The Congressional Budget Office (CBO) estimated that fiscal year 2024 federal receipts totaled $4.92 trillion, and outlays totaled $6.75 trillion, resulting in a $1.83 trillion budget deficit (6.4% of GDP). CBO projects deficits will decline in the near-term, primarily due to the assumption that the expiration of the individual income tax provisions of the TCJA occurs as scheduled.

Extension of the expiring provisions of the TCJA alone would add about $5 trillion to the debt over the following 10 years. However, even under the assumption that TCJA provisions and other current-law temporary tax provisions will expire, future deficits are expected to increase from a low of 5.2% of GDP in 2027 to 8.5% of GDP by 2054. Net interest payments are expected to more than double from 3.1% of GDP in 2024 to 6.3% of GDP by 2054.

Figure 4: Projected increases in net federal interest payments



Source: Congressional Budget Office

The "Department of Government Efficiency"

The objective of the incoming Trump Administration's Department of Government Efficiency (DOGE), the presidential advisory commission led by businessmen Elon Musk and Vivek Ramaswamy, is to streamline the federal government by reducing inefficiency and decreasing the federal fiscal budget by cutting federal spending. The DOGE reportedly is looking to trim approximately $2 trillion from the government's budget by reducing waste, abolishing redundant agencies, and downsizing the federal workforce.

Observation: It is unclear whether this $2 trillion amount is an annual or longer-term target. In more recent statements, Elon Musk stated that "we'll try for $2 trillion," which might be "the best-case outcome." Musk commented that "we've got a good shot" at getting $1 trillion in cuts." The DOGE does not appear to be considering or proposing revenue-raising options, in contrast with some previous streamlining efforts.

It remains to be seen what the Trump administration and Congress will do with the DOGE's recommendations. Republican House leaders recently announced plans to establish a Delivering on Government Efficiency Subcommittee within the House Oversight and Accountability Committee to be chaired by Rep. Marjorie Taylor Green (R-GA) to work closely with the DOGE to reduce governmental spending. In addition, the House and Senate have formed DOGE caucuses.

Observation: Any executive order to impound federal funds that Congress has appropriated or other legal mechanism that President Trump may attempt to use to accomplish the DOGE's goals by circumventing Congress will need to be considered in the context of the rules of the Budget and Impoundment Control Act of 1974 (BICA) and previous court rulings.

Several court cases were brought challenging President Richard Nixon's executive actions related to impounding federal funds appropriated by Congress. Although decided after the BICA was enacted, the Supreme Court unanimously held in *Train v. City of New York* that even without BICA, the president does not have unilateral authority to impound funds that had been appropriated as part of bills enacted by Congress. The Trump administration could seek to have this issue reconsidered by the current Supreme Court.

Executive actions around cutting government spending produce direct and indirect fiscal consequences in terms of receipts and outlays, as scored by the Office of Management and Budget (OMB) and Treasury. Any proposals producing mandatory savings and additional revenue could be eligible for budget reconciliation legislation should Congress decide to do so. However, such proposals would be subject to reconciliation restrictions under Senate Byrd rules, as discussed below. Legislated changes on discretionary spending items likely could be implemented though the use of regular order appropriations bills.

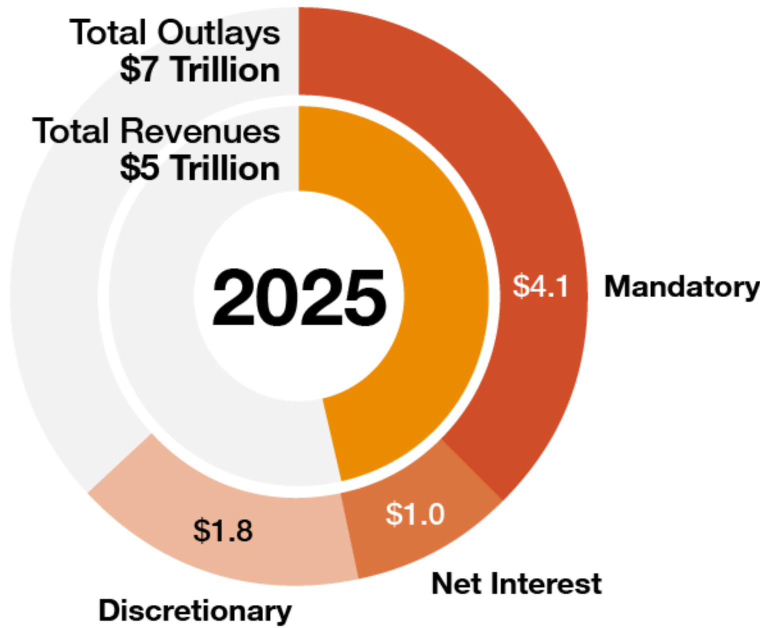
For more on previous attempts to streamline the federal government, see Appendix D.

To put the DOGE's stated objectives in context, CBO is projecting that total federal government expenditures for fiscal year 2025 will be $7 trillion, with $4.1 trillion in mandatory spending, $1.8 trillion in discretionary spending, and $1 trillion in interest payments on the federal debt. Social Security and Medicare are the two largest mandatory spending programs, and military spending accounts for more than half of all discretionary spending appropriated by Congress.

In 2024, there were approximately 2.2 million federal civilian employees, with roughly 796,000 of these civilian employees working for the Defense Department and related agencies. The number of federal civilian employees peaked at 3 million in 1990.

For examples of potential deficit reducing measures identified by CBO staff, see Appendix E.

Figure 5: Projected FY 2025 federal outlays and revenues



Source: Congressional Budget Office

Balance of power

House of Representatives

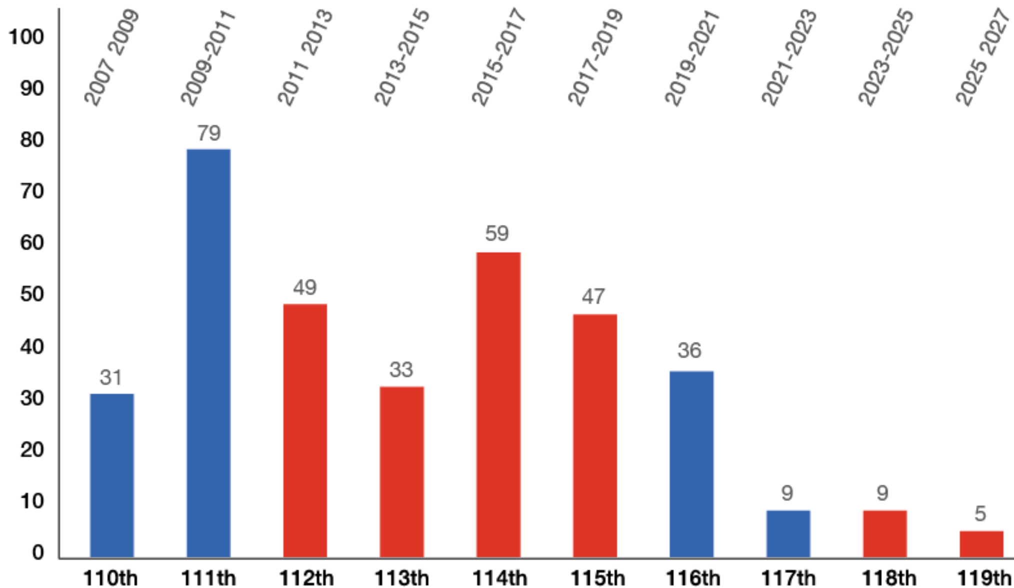
After the 2024 elections Republicans retained a slim majority in the House of Representatives, with 220 Republicans and 215 Democrats elected. Democrats gained a net of one seat. The Republican majority temporarily will become even smaller — 217 to 215 — with three Republican House seats becoming vacant early in the new Congress.

Special elections will be held April 1, 2025, in two Florida districts to fill vacancies left by Rep. Michael Waltz (R), who is expected to resign January 20 to become National Security Adviser in the Trump administration, and former Rep. Matt Gaetz (R), who resigned from the House last November and then withdrew from being considered by the Senate to serve as Attorney General while also declining to serve in the House after being re-elected. A special election in New York has not yet been scheduled to fill the seat of Rep. Elise Stefanik (R), who is expected to resign if confirmed by the Senate to become UN ambassador.

Rep. Mike Johnson (R-LA) continues to serve as Speaker of the House and Rep. Hakeem Jeffries (D-NY) again will serve as House Minority (Democratic) Leader.

Observation: With Republicans holding an even slimmer House majority at the start of 2025 than they did last year, Speaker Johnson is expected again to face the challenge of trying to unite Republicans behind key priorities, with no room for error. Nearly unanimous support among Republicans will be required to pass legislation that lacks bipartisan support. A key difference in 2025 will be the presence of a Republican president in the White House.

Figure 6: House majorities have narrowed in the past several Congresses



Source: US House

Senate

Republicans achieved a 53 to 47 seat majority in the Senate as a result of the 2024 elections, with a net gain of four seats. The Senate convened with 52 Republicans and 47 Democrats (including the two Independents who caucus with Democrats); West Virginia Governor and Senator-elect Jim Justice (R) delayed resigning as governor and taking his Senate seat until his successor took office on January 13.

Senator JD Vance (R-OH) resigned from the Senate on January 10 to become Vice President and Ohio governor Mike DeWine (R) will appoint a successor for the seat until 2026, when an election will be held for the remaining two years of the term. In addition, Senator Marco Rubio (R-FL) is expected to resign if confirmed to serve as Secretary of State in the Trump administration. Florida Governor Ron DeSantis (R) will appoint a replacement until 2026, when an election will be held for the remaining two years of the term.

Senator John Thune (R-SD) was selected to serve as new Senate Majority Leader, succeeding Senator Mitch McConnell (R-KY), who stepped down from his Senate Republican leadership position after a record-breaking 18-year tenure as leader. Former Senate Majority Leader Chuck Schumer (D-NY) will serve as Senate Minority (Democratic) Leader.

Senate procedures generally require 60 votes to limit debate on legislation and bring about a vote on final passage. A Senate rule modification adopted in 2017 lowered the threshold for approving US Supreme Court nominations to a simple majority (usually 51 votes), which brought the requirement in line with a 2013 rule change that adopted a simple majority threshold for executive branch and non-Supreme Court judicial nominations. Efforts in a previous Congress to alter the legislative filibuster were unsuccessful. Senate Majority Leader Thune vowed to retain the current super-majority requirement in his opening remarks for the 119th Congress.

Senate rules allow for a simple majority vote to enact budget reconciliation legislation, instead of the 60 votes generally required for legislation. A reconciliation bill must comply with several requirements to preserve the protection against needing 60 votes in the Senate, as discussed below.

House and Senate tax committees

Rep. Jason Smith continues to serve as chairman of the House Ways and Means Committee, and Rep. Richard Neal (D-MA) is the Ranking Democratic Member. The Ways and Means Committee currently is composed of 26 Republicans and 19 Democrats.

The new Republican members on the committee this Congress are Reps. Aaron Bean (FL), Max Miller (OH), Nathaniel Moran (TX), and Rudy Yakym (IN). Three Democratic members are returning to the committee — Del. Stacey Plaskett (VI) and Reps. Brendan Boyle (PA) and Tom Suozzi (NY).

The Senate Finance Committee is led by new Chairman Mike Crapo (R-ID) and Senator Ron Wyden (D-OR) serves as the Ranking Democratic Member. The Finance Committee includes 14 Republicans and 13 Democrats. Roger Marshall (KS) is the only new Republican on the committee. The new Democratic members are Bernie Sanders (I-VT), Tina Smith (MN), Ben Ray Luján (NM), Raphael Warnock (GA), and Peter Welch (VT).

Eight members of the Finance Committee hold seats that are up for election in 2026, including Republicans Bill Cassidy (LA), John Cornyn (TX), Steve Daines (MT), Roger Marshall (KS), and Thom Tillis (NC) and Democrats Ben Ray Luján (NM), Tina Smith (MN), and Mark Warner (VA).

Administration

The President has the power to veto legislation passed by Congress, with a two-thirds majority of both the House and Senate required for a veto override. With Republicans holding majorities in both the House and Senate, the Presidential veto is not likely to be an important factor in the current Congress.

Scott Bessent has been nominated to serve as Treasury Secretary. Former Joint Committee on Taxation (JCT) chief of staff and former Ways and Means Republican chief tax counsel Ken Kies has been nominated to serve as Treasury Assistant Secretary for Tax Policy.

President Trump has nominated former Republican Congressman Billy Long to serve as IRS Commissioner. Current Commissioner Daniel Werfel has been serving as IRS Commissioner since March 2023 and his term is not scheduled to expire until November 2027.

President Trump's economic team appointments include Kevin Hassett, Director of the National Economic Council; Russell Vought, Director of the Office of Management and Budget (OMB); and Stephen Miran, Chair of the Council of Economic Advisers.

In the trade area, President Trump has nominated Howard Lutnick for Commerce Secretary and Jamieson Greer is his nominee for United States Trade Representative.

A listing of key policymakers is provided in Appendix A.

Looking ahead to the 2026 midterm elections

All 435 seats in the House are up for election every two years. Democrats would need to achieve a net gain of only three seats in the 2026 elections to regain control of the House. This assumes seats vacated due to resignation will be filled by members of the same party in special elections before general elections are held for seats in the next Congress. In the last several midterm elections for a second-term president, the president's party has lost an average of 20 House seats.

Observation: In the 2024 election there were a small number of so-called "crossover" House districts where candidates in one party were elected to House seats in districts won by the opposing party's presidential nominee. At least 13 Democrats were elected in districts President Trump won, while three Republicans were elected in districts Vice President Kamala Harris won.

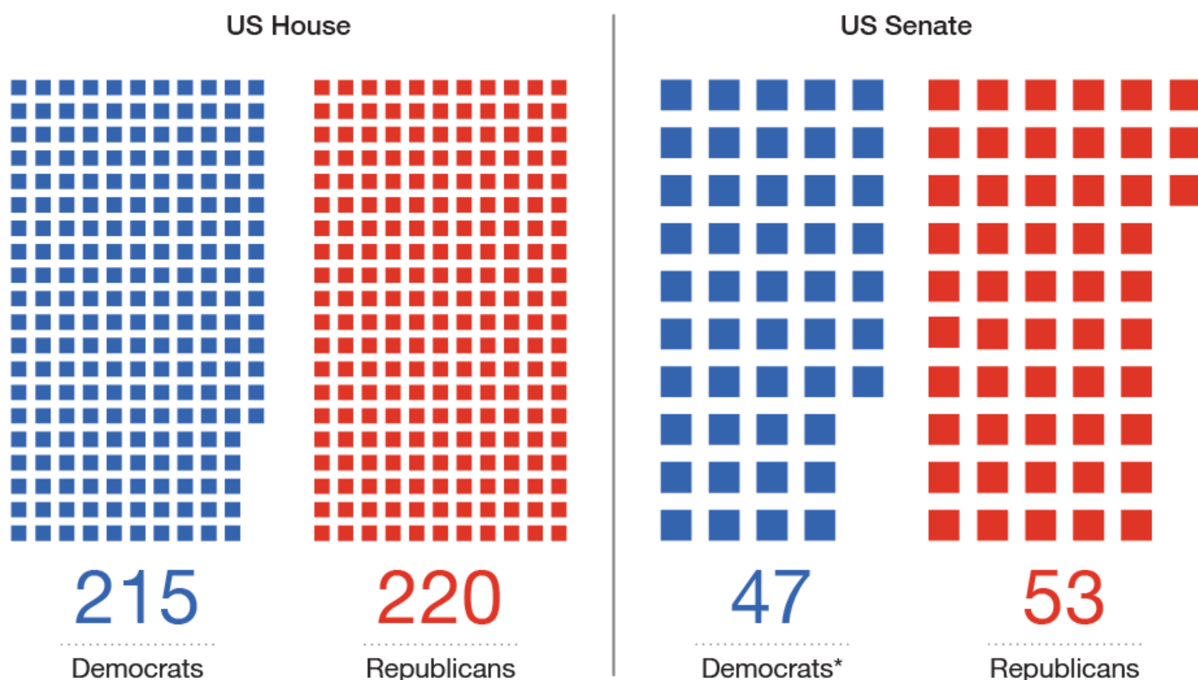
As of this writing, one House member, Rep. Raúl Grijalva (D-AZ), has announced he will not seek re-election in 2026.

Democrats would need a net gain of four seats in the 2026 elections to regain control of the Senate. Roughly one-third of all Senate seats are subject to election every two years. In 2026, 33 Senate seats are up for re-election, of which 13 currently are held by Democrats and 20 currently are held by Republicans. In addition, special elections will be held for the Ohio Senate seat that was held by JD Vance and the Florida Senate seat held by Marco Rubio for the two years remaining in those terms.

Observation: Of the 33 Senate seats up for election in 2026, 21 are in states won by President Trump in the 2024 presidential election and 12 are in states won by Vice President Harris.

A listing of all Senators whose seats are subject to election in 2026 is included in Appendix B.

Figure 7: House and Senate 2024 election results

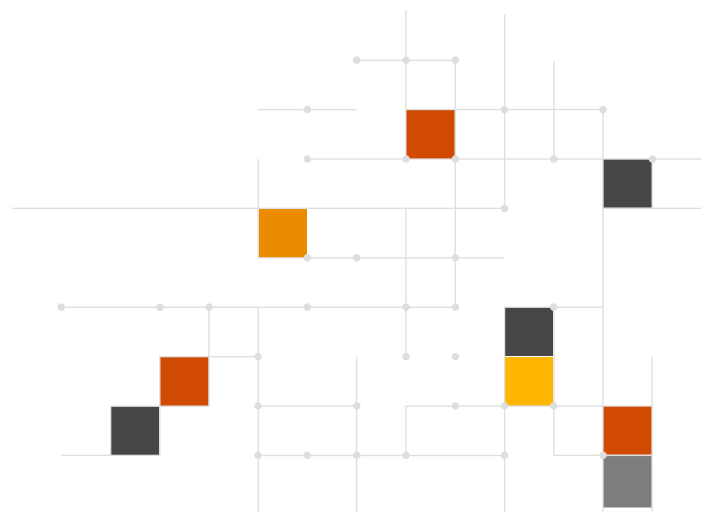


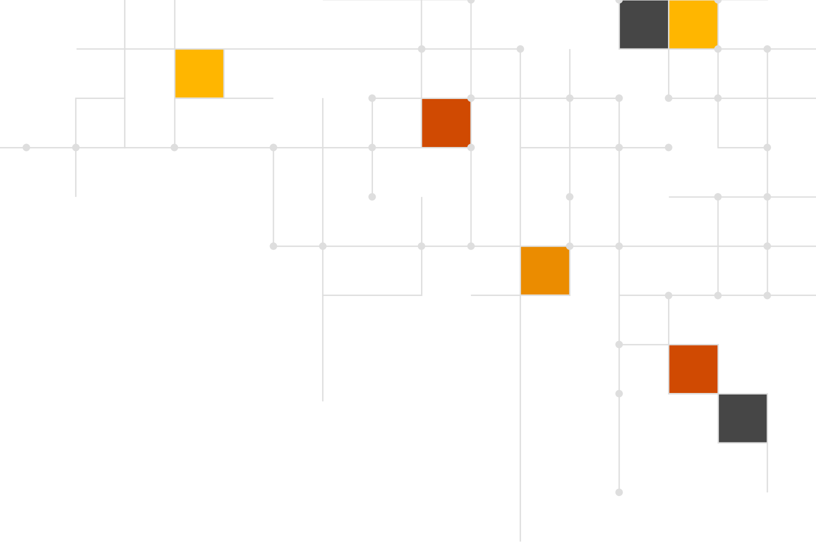
*Includes two Independents: Senators Bernie Sanders (I-VT) and Senator Angus King (I-ME)

Source: US Congress

Figure 8: 2025 Congressional legislative schedule

House and Senate convene	January 3
Martin Luther King Jr. Day Presidential inauguration	January 20
President's address to a joint session of Congress	TBD
House recess	January 27 - February 3
President's Day recess (House)	February 14 - 21
President's Day recess (Senate)	February 14 - 17
House recess	March 13 - 21
Senate recess	March 17 - 21
Spring recess (House and Senate)	April 14 - 25
Memorial Day recess (House and Senate)	May 26 - 30
House recess	June 16 - 20
Juneteenth	June 19
Independence Day recess (House and Senate)	June 30 - July 4
August recess (House)	July 25 - September 1
August recess (Senate)	August 4 - September 1
House and Senate recess	September 22 - 26
House recess	October 1 - 3
Senate recess	October 2 - 3
Senate recess	October 13 - 17
Veterans' Day recess (House and Senate)	November 10 - 14
Thanksgiving recess (House and Senate)	November 24 - 28
Target adjournment date (House)	December 18
Target adjournment date (Senate)	December 19





US tax policy outlook

President Trump is expected to seek enactment of key tax proposals that he advanced during the 2024 campaign season. These proposals include extending TCJA individual tax provisions and various business tax provisions that are scheduled to expire, as noted below in Figure 9.

Business tax proposals announced by President Trump include:

- lowering the 21% corporate income tax rate to 15% for companies producing goods in the United States,
- reinstating 100% 'bonus' depreciation,
- restoring Section 174 expensing for US-based research activities, and
- increasing the current 1.4% excise tax on the net investment income of certain university endowment funds.

Individual tax relief proposals announced by President Trump include:

- eliminating taxes on tip income,
- eliminating taxes on certain Social Security benefits,
- eliminating taxes on overtime pay,
- eliminating taxes on Americans abroad,
- providing a tax credit for unpaid family caregivers,
- allowing a deduction for auto loan interest payments, and
- restoring federal individual itemized deductions for state and local taxes.

The incoming Trump administration's Treasury Department will be expected to submit to Congress specific details on the president's tax proposals.

Observation: The incoming Trump administration's Treasury Department will be expected to submit to Congress specific details on the president's tax proposals. While Republicans in Congress are expected generally to support President Trump's policy goals, it is up to the House and Senate to draft statutory tax legislation that would need to balance the goal of extending TCJA provisions and proposals to enact new tax cuts.

House and Senate Republicans have announced that they intend to use budget reconciliation procedures to address expiring TCJA tax provisions and President Trump's tax proposals with only Republican votes, as discussed below.

Other temporary current-law tax provisions include Affordable Care Act premium assistance tax credits and the work opportunity tax credit that are set to expire at the end of 2025 and various Inflation Reduction Act clean energy tax credits that are set to expire in 2032 (with some transition dates).

Based on Joint Committee on Taxation estimates, the 2026 to 2035 10-year net cost of extending all tax provisions set to expire or scheduled to change would add more than $5.5 trillion to the $22 trillion of increased federal debt that CBO has projected through 2035 under current law for federal spending and tax policies. TCJA individual provisions altogether account for nearly $4 trillion of this projected revenue cost effect.

Some economists projected last year that President Trump's campaign tax proposals would increase this amount to over $7 trillion. The revenue effect of campaign proposals that go beyond the TCJA, and even reverse some of TCJA's base broadening, was estimated to have a significant effect on the federal debt.

The previous 118th Congress attempted to address some of the TCJA provisions included in President Trump's campaign tax proposals that already have been subject to scheduled changes since 2017. However, the Senate last August blocked a House-passed bill (H.R. 7024) that would have restored through the end of 2025 on an elective retroactive, seamless basis 100% 'bonus' depreciation under Section 168(k) and expensing for US-based R&D investments under Section 174, as well as reinstating the EBITDA-based business interest limitation under Section 163(j). These provisions are expected to be considered on a prospective basis as part of a 2025 reconciliation tax bill.

H.R. 7024 also featured provisions to enhance the child tax credit, provide disaster tax relief, and provide relief from US-Taiwan double taxation. Enhancements to the child tax credit could be addressed as part of a 2025 reconciliation tax bill since the doubling of the credit is one of the TCJA provisions subject to sunset. US-Taiwan legislation also could be considered this year, as discussed below. The previous Congress did enact a separate bill (H.R. 5863) to provide tax benefits to victims of certain natural disasters — including hurricanes, wildfires, and the East Palestine, Ohio train derailment — that previously had been included in H.R. 7024.

Figure 9. Key TCJA tax provisions set to expire or change

Key TCJA individual tax provisions scheduled to expire Dec. 31, 2025 include:		
	From in 2025	To in 2026
All current individual tax rates	37% for top individual ordinary income rate	39.6% for top individual ordinary income tax rate
Pass-through business income deduction	20%	0%
Enhanced child tax credit	$2,000	$1,000
Higher standard deductions	**From in 2025**	**To in 2026**
Married filing jointly	$30,000	$16,700
Heads of household	$22,500	$12,250
Single filers	$15,000	$8,350
Limits to itemized deductions		
State and local income tax deduction	$10,000 cap	Unlimited
Mortgage interest deduction	$750,000 cap	$1,000,000
Estate and gift tax exemption		
Single	$13,990,00	$7,000,000 estimated adjusted for inflation
Married couples	$27,980,000	$14,000,000 estimated adjusted for inflation
Other provisions set to sunset Dec. 31, 2025, include expanded individual alternative minimum tax relief provisions.		

Key corporate rates scheduled to increase automatically in 2026 include:		
	From in 2025	**To in 2026**
GILTI tax rate on certain foreign earnings	10.5%	13.125%
BEAT minimum tax on US earnings	10%	12.5%
Favorable rate on FDII eligible income	13.125%	16.4%

Look-through treatment for certain foreign corporation income is also set to expire at the end of 2025.

Source: CBO, Update to the Budget and Economic Outlook: 2024 to 2034, June 2024, Tax Parameters Supplemental Data; IRS, Rev. Proc. 2024-40, October 22, 2024.

Step one: Approve a budget resolution providing instructions for a reconciliation tax bill

The first critical test for a 2025 reconciliation tax bill will be whether House and Senate Republicans will vote for a budget resolution providing instructions that will set forth the projected impact of a final reconciliation tax bill on the national debt. This vote will need to be nearly unanimous given the narrow majorities in the House and Senate.

Reconciliation instructions will provide the fiscal framework under which the House Ways and Means Committee and the Senate Finance Committee will draft a tax bill to extend TCJA tax provisions and address tax proposals advanced by the Trump administration and Republican members of Congress.

Both parties have regularly used reconciliation procedures to enact major tax bills when they have controlled both the White House and Congress, as shown in Figure 10, but the scope of such legislation is limited by Senate reconciliation rules. Reconciliation procedures were originally established in the 1980s to facilitate the enactment of legislation to reduce federal budget deficits through a combination of mandatory spending cuts and revenue increases.

Current law or current policy?

The House and Senate budget committee chairs have significant discretion to adopt budgetary baselines and economic assumptions that would be reflected in reconciliation instructions. A key decision to be made during the budget resolution process is whether a 2025 tax bill will be considered under the traditional "current-law" baseline that has been used for previous reconciliation bills or under a "current-policy" baseline that has been used periodically for tax bills under regular legislative procedures that generally require a 60-vote majority in the Senate.

The 2017 TCJA was enacted using budget reconciliation procedures under a joint House and Senate budget resolution that set a $1.5 trillion deficit-financing cap on the legislation for the initial 10 years covered by the resolution. By using a current-law baseline, Republicans in 2017 were able to count the budget savings of the scheduled December 31, 2025, sunset of individual tax provisions and other scheduled changes to business provisions. These budget savings under a current-law basis were adopted both to remain under the $1.5 trillion cap on initial deficit financing and to comply with the prohibition on reconciliation legislation resulting in a long-term deficit increase outside the period covered by budget resolution.

For a 2025 tax reconciliation bill, Senate Finance Committee Chairman Crapo and House Ways and Means Chairman Smith have called for using a current-policy baseline that would assume the cost of extending the TCJA within a revised CBO projection of the federal debt. Under present law, CBO still would be required to project the revenue effect of the legislation under a current-law baseline as an addition to the national debt.

Proponents of using a current-policy baseline argue that extending a temporary tax cut should not be counted as a new tax relief measure but instead merely avoids allowing a scheduled tax increase to take effect. Under this current-policy baseline approach, only new tax proposals, such as those proposed by President Trump or modifications to current TCJA tax policies, would be considered to require either offsetting spending reductions or tax increases or to be explicitly deficit financed.

Observation: A current-policy baseline has been used periodically for tax bills under regular legislative procedures that generally require a 60-vote majority in the Senate, as noted above. The use of this approach by Republicans to pass reconciliation tax bills in the Senate by a simple majority would set a new precedent that Democrats could use in the future.

A current-policy baseline was used most significantly in 2012 under regular legislative procedures when then-President Barack Obama and Congress enacted a bipartisan “fiscal cliff” tax bill that extended over 80% of the temporary reconciliation tax cuts originally enacted in 2001 and 2003 under President George W. Bush. President Obama’s budget assumed a policy baseline that included the cost of preserving the entirety of the Bush tax cuts and claimed a deficit reduction effect for allowing the Bush tax cuts to lapse for higher-income individuals.

The Obama Administration defended the use of a current policy baseline in a blog post on January 1, 2013, arguing that “the relevant point of comparison isn't current law, it is current policy” – those policies that were in place on December 31st, the day before all of these changes were scheduled to take effect. Different organizations, ranging from the Bowles-Simpson Fiscal Commission to the House Budget Committee, have considered this current policy baseline to be the appropriate reference point, since it measures changes relative to the status quo, rather than the mix of expiring provisions and policy changes that would likely never be implemented.” This post was authored by then-OMB Deputy Director for Management Jeff Zeints, who later went on to become President Biden’s Chief of Staff.

Observation: President Obama’s use of a current-policy baseline did not eliminate the effect of extending most of the Bush tax cuts on the federal debt. CBO and JCT at the time estimated that the 2012 legislation added more than $4 trillion to the national debt, which was $16 trillion at the time. Similarly, the use of a current-policy baseline for a 2025 reconciliation tax bill will not eliminate the effect of the final legislation on the current $36 trillion national debt.

In addition to setting a new precedent for future reconciliation tax bills, the use of a current-policy baseline would require certain modifications to TJCA provisions to comply with Senate reconciliation “Byrd rules” that were established under former Senate Majority Leader Robert Byrd (D-WV). A critical Byrd rule is that individual provisions in a reconciliation bill must have a budgetary effect that is more than incidental to be protected from procedural challenges that would require 60 votes to overcome.

To satisfy this specific Byrd rule, each of the more than 40 separate current-law expiring TCJA individual tax provisions that would be assumed to be extended with no budgetary effect under a current-policy baseline would need to be modified so that a measurable budgetary effect results.

For example, each individual income tax bracket would need to be modified to produce a budgetary effect (e.g., the current $626,350 threshold at which the top 37% individual tax bracket applies to single filers in 2025 could be lowered to $600,000 for 2026 and future years in a manner that would be scored as a revenue increase). Modifications to expiring TCJA provisions that are scored as increasing revenue in this manner could then be used to offset part of the cost of new tax cuts proposed by President Trump or Republicans in Congress.

Observation: The Byrd rule against increasing deficits in future years outside the customary 10-year budget window could be held to apply only to new tax cuts that are not fully offset. Under a current-policy baseline approach, the original TCJA tax provisions that have been modified could be deemed to be "permanent" and only new tax cuts would be subject to a mandatory sunset at some point within the budget window. This could potentially protect the bill from a 60-vote procedural challenge that the legislation violates this particular Byrd rule. Of course, no tax provision can be considered truly permanent since a future Congress can revisit any provision of the tax code.

Senate parliamentarian Elizabeth MacDonough is expected to play a critical role in how Senate reconciliation rules and precedents affect the consideration of a 2025 tax bill. Rulings by the parliamentarian could affect both the crafting of reconciliation instructions — including the question of how to apply a current-law or current-policy baseline — and in reviewing drafts of legislative proposals to be considered during Senate floor debate on a reconciliation tax bill. For example, MacDonough ruled in 2021 that a Democratic proposal to increase the minimum wage violated the Byrd rule against using reconciliation procedures to advance policy changes that have a merely incidental budgetary effect, so the proposal was dropped from the American Rescue Plan reconciliation legislation.

Rulings by the parliamentarian can be appealed but are generally respected in terms of applying Senate rules consistently regardless of which party controls the Senate. However, a previous Senate parliamentarian, Robert Dove, was forced out of the position in 2001 by Senate Republican leaders in response to rulings that were considered to be obstacles to advancing a reconciliation tax bill under then-President George W. Bush.

Observation: The question of whether a 2025 tax reconciliation tax bill is considered under a current-law baseline or a current-policy baseline could depend ultimately on which approach can secure the near-unanimous support of House and Senate Republicans, including those members who consider themselves to be "deficit hawks." Last December, for example, Rep. Chip Roy (R-TX) stated that "you are not getting tax cuts [in 2025] without corresponding, significant spending cuts that will reduce deficits."

Support for a budget resolution with reconciliation instructions also could be affected by the mix of other policy goals that might be addressed as part of a 2025 reconciliation bill. For example, reconciliation instructions could call for cuts in Medicaid, food assistance, student loans, or other mandatory spending programs that are intended to produce budget savings that would partially offset the cost of various tax provisions. The critical question will be whether specific mandatory spending reductions would help to secure Republican votes for the final legislation or would lose votes in the narrowly divided House and Senate.

President Trump has stated that revenue from higher tariffs could be used to offset some of the cost of his tax proposals. While a president can impose tariffs under many conditions (e.g., unfair trade practices) without Congress, as discussed below, reconciliation procedures generally would require legislative action to impose higher tariff rates for the resulting revenue increase to be officially counted as an offset for other provisions in a reconciliation bill.

Observation: It is unclear whether Congressional Republicans will want to vote on specific tariff measures that might increase the price of goods purchased by their constituents. While the revenue effect of higher tariffs that President Trump could impose under existing authority might not be included by CBO in the official score for a reconciliation tax bill, some Republicans could choose to consider the revenue from higher tariffs as helping to address their broader concerns about the size of the national debt.

Figure 10: Reconciliation tax bills have become the norm when one party controls the White House and Congress

	White House	House	Senate	
107th Congress (2001-2003)*				Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L.107-16)
108th Congress (2003-2005)				Jobs and Growth Tax Relief Reconciliation Act of 2003 (P.L. 108-27)
109th Congress (2005-2007)				Deficit Reduction Act of 2005 (P.L. 109-171) Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222)
110th Congress (2007-2009)				
111th Congress (2009-2011)				Health Care and Education Reconciliation Act of 2010 (P.L. 111-152)
112th Congress (2011-2013)				
113th Congress (2013-2015)				
114th Congress (2015-2017)				
115th Congress (2017-2019)				The Tax Cuts and Jobs Act of 2017 (P.L. 115-97)
116th Congress (2017-2019)				
117th Congress (2021-2023)				American Rescue Plan Act of 2021 (P.L. 117-2) The Inflation Reduction Act of 2022 (P.L. 117-169)
118th Congress (2023-2025)				
119th Congress (2023-2025)				?

* Democrats gained control of the 50-50 Senate mid-session following enactment of the 2001 reconciliation tax bill, after then-Republican Senator Jim Jeffords of Vermont became an Independent and caucused with Senate Democrats.

Step two: Craft a reconciliation tax bill that can clear the House and Senate with near-unanimous support

Once a joint budget resolution with reconciliation instructions has been approved by Congress, the House and Senate tax committees and other committees in each chamber with responsibilities under the budget resolution would be charged with drafting legislation. The broad scope of reconciliation instructions under an FY 2025 budget resolution addressing tax issues as well as border security, energy production, and reductions in mandatory spending is expected to require the input of many House and Senate committees. The resulting legislation both must be consistent with the reconciliation instructions to advance in the Senate without being at risk of a potential 60-vote challenge and must be able to gain the support of nearly all House and Senate Republicans.

In this environment, the House Ways and Means Committee and the Senate Finance Committee will need to consider a host of competing interests over various tax issues. Potential areas of focus for Congressional Republicans may include:

- **The cost and scope of certain tax cut proposals offered by President Trump.** Many Republicans in Congress have expressed support for exempting certain tip income or overtime pay from taxation but have indicated that the scope of such exemptions might need to be narrowly defined to limit the proposals' revenue cost and to avoid unintended tax avoidance. Reconciliation rules include a prohibition against proposals that affect Social Security, so this is expected to be an obstacle for President Trump's proposal to repeal the current tax on certain Social Security benefits.

- **The fate of Inflation Reduction Act energy tax credits.** During his campaign, President Trump called for repealing many of the clean energy tax credits that were enacted as part of the 2022 Inflation Reduction Act. At the same time, 18 House Republicans signed a letter last year expressing opposition to full repeal of clean energy provisions that are promoting business investment in their districts. While House Speaker Johnson and other Republican leaders have indicated that a full "repeal and replace" approach to the Inflation Reduction Act provisions appears unlikely, they have expressed an interest in prospective efforts to address the rising cost of the clean energy incentives. JCT has projected the cost of the Inflation Reduction Act tax credits to have increased from the original $270 billion estimate to more than $650 billion through FY 2033. The 2022 Inflation Reduction Act also provided an additional $100 billion in clean energy grant incentives.

- **State and local taxes (SALT) cap relief.** President Trump has called for repealing the $10,000 cap on itemized individual federal income tax deductions for state and local taxes. Key Republican leaders have noted that repealing the current SALT cap fully would be costly — more than $1 trillion by some estimates — and that the cap remains popular with many Congressional Republicans since it was adopted in 2017 as an offset for TCJA tax cut measures like an expanded standard deduction and alternative minimum tax relief. Some Republicans have indicated that a doubling of the $10,000 cap to $20,000 for joint filers might be considered, but it remains unclear if this level of SALT cap relief will be sufficient for House Republican members from states that have high state and local taxes.

These are only a few examples of issues that will need to be considered by the House and Senate tax committees. The cumulative revenue effect of any final bill also will have to be acceptable to House and Senate Republicans who are concerned about the size of the federal debt.

Business tax provisions

Advancing pro-growth business tax policies has been identified as a top priority by the incoming Trump administration and Congressional Republicans. It remains to be seen what steps the House and Senate tax committees may take in response to business tax proposals that include lowering the 21% corporate income tax rate to 15% for companies producing goods in the United States, preserving the 20% deduction for certain pass-through business income, reinstating 100% bonus depreciation, and reinstating Section 174 expensing for research activities.

Observation: In the case of the proposed 15% corporate rate for companies producing goods in the United States, some analysts have suggested that the Section 199 domestic manufacturing deduction, which was repealed by the TCJA, could be a model for providing a tax reduction for the eligible income of qualifying companies.

The House and Senate tax committees are expected to consider potential changes to US international tax rules, including proposals to turn off scheduled changes to the GILTI, BEAT, and FDII tax provisions that were enacted as part of the TCJA. The committees also could seek to address concerns about the potential for US companies to pay a higher overall tax rate to other governments under the new Pillar Two global minimum tax regime, as discussed in more detail below.

Observation: It is doubtful whether the Republican-controlled Congress will devote limited federal fiscal resources to repealing the corporate alternative minimum tax or other revenue-raising measures that were enacted as part of the 2022 Inflation Reduction Act.

The House and Senate tax committee could consider some revenue-raising provisions affecting business or high-income individuals to offset part of the cost of a 2025 tax bill. For example, some in Congress have suggested that SALT cap relief for middle-class taxpayers could be offset by limitations on the corporate deduction for state and local business taxes or by measures that would shut down pass-through entity tax regimes established by most state governments to allow certain qualifying partners to claim a SALT deduction benefit at the partnership level.

It is unclear whether the House and Senate tax committees might consider modified versions of some revenue raisers previously proposed by the Biden administration, such as the proposals to increase the federal excise tax on certain stock repurchases, to expand Section 162(m) rules denying deductions for compensation in excess of $1 million, or to change to the tax treatment of partnerships and carried interest.

Observation: While an increase in the 21% US corporate income tax rate appears unlikely, fiscal and political pressures could lead Congress to adopt some revenue-raising offsets for a tax bill that could degrade the domestic investment environment.

Finally, the House and Senate tax committees could again adopt sunsets of tax relief measures or scheduled increases in certain tax provisions affecting individual or business taxpayers to comply with budget reconciliation instructions. Such measures were used extensively in 2017 to comply with budget reconciliation instructions for the TCJA.

Observation: In setting the duration of any potential tax relief sunsets or scheduled tax increases, House and Senate Republicans may want to consider recent trends in how party control has shifted more frequently in recent years. Presidents since Clinton have enjoyed control of the House and Senate by their same party for at least the first two years of their terms, but divided government generally has returned following midterm elections. In case Democrats were to gain control of the White House and Congress following the 2028 federal elections, consideration might be given in a 2025 tax reconciliation bill to setting any future tax provision sunsets to take effect after the 2030 midterm elections when Republicans might anticipate securing a seat at the table in what could be a return to divided government.

Potential tax regulatory developments

Although the incoming Trump White House and Treasury Department will likely focus significantly on potential tax legislation in 2025, regulatory developments also are likely to demand attention from policymakers and taxpayers.

The incoming Trump Administration will face a dramatically altered regulatory landscape as a result of the Supreme Court's recent decision in *Loper Bright Enterprises v. Raimondo*, 603 U.S. 369 (2024). *Loper* overturned the *Chevron* doctrine, which had been in place for 40 years and generally required courts to defer to an administrative agency's regulatory interpretation of a statute unless the agency interpretation was considered unreasonable. Without *Chevron* deference, there is an increased likelihood of taxpayer challenges to regulatory guidance where that guidance is not clearly consistent with the associated statutory text or supported by an explicit grant of authority given by Congress to Treasury. It remains to be seen to what extent the incoming Trump Administration's approach to future regulatory guidance will be affected by *Loper*.

In addition, while there is typically a pause in regulatory guidance following the inauguration of a new president (particularly given that President Trump is not from the same political party as his predecessor), both taxpayers and the government will continue to depend on regulations to provide guidance to resolve ambiguities and facilitate compliance.

Of particular note, Treasury issued proposed regulations for the corporate alternative minimum tax (CAMT) in September 2024, just over two years after Congress enacted it. The CAMT statutory text leaves many fundamental questions unanswered and provides multiple grants of authority to Treasury to resolve issues and provide guidance. More recently, Treasury issued proposed regulations in November 2024 addressing certain issues associated with previously taxed earnings and profits (PTEP). PTEP assumed significantly greater importance to many taxpayers following the enactment of the TCJA and the introduction of the GILTI regime, but the existing final regulations have not been substantively revised since the 1960s.

In these and other areas, the incoming Trump Administration and Treasury will have to pick up the work that began under the Biden Administration and determine whether to follow the same general approach of its predecessors or make a meaningful change in direction. Affected taxpayers should consider whether the change in administration might present an opportunity for further engagement on proposed regulations, even if the comment period has formally closed or the taxpayer has previously submitted comments.

The US Internal Revenue Service: Top five areas to watch in 2025

Changes in IRS leadership

President Trump has announced plans to nominate former Representative Billy Long (R-MO) to serve as IRS Commissioner. A December 4 announcement indicated that Trump intends to break with precedent and remove current IRS Commissioner Daniel Werfel, who was appointed by President Joe Biden in 2022, from the position.

Although IRS Commissioners can be removed at the president's will, it is unusual for them to be asked to leave office before the end of their term. In fact, the replacement of Werfel with Long would be the first time since the five-year term was codified in 1998 that a sitting IRS Commissioner has been removed as the result of a change in administration.

Under the five-year term codified in the IRS Restructuring and Reform Act, Werfel's term is set to expire in November 2027. If Trump removes Werfel immediately after his inauguration, an acting commissioner will need to be appointed until Long is confirmed by the Senate. If confirmed, Long would be slated to serve the remainder of Werfel's five-year term.

During his time in Congress, Long several times cosponsored the Fair Tax Act, which would have abolished the IRS and replaced the federal income tax with a national sales tax to be collected and remitted to Treasury by state administrators. Long also backed bills that would have prevented IRS employees from organizing, collective bargaining, and participating in labor organizations.

Trump also will appoint a new IRS chief counsel to replace Marjorie Rollinson who was confirmed by the Senate in March 2024 and has announced that she plans to retire before the end of the Biden Administration.

Observation: IRS chief counsel Rollinson expressed concerns about a significant increase in the complexity of federal tax regulations in public remarks last December.

The Senate Finance Committee will be responsible for vetting and holding hearings on both the IRS commissioner and chief counsel nominations. Republican committee members have indicated that they will be seeking answers on Long's position on IRS enforcement and how he would advance the agency's modernization efforts.

IRS funding

IRS funding and tax administration are expected to be areas of focus for the incoming Trump administration and Congressional Republicans. The Republican-led House and Senate appropriations committees are expected to reduce or eliminate the Inflation Reduction Act's remaining multiyear funding for IRS enforcement and operations.

The 118th Congress rescinded $21.6 billion of the original $80 billion in multiyear Inflation Reduction Act funding for the IRS to increase enforcement. The recissions made to date have reduced to $24 billion the $45.6 billion initially provided by the Inflation Reduction Act for IRS enforcement.

Congress on December 21 completed action on another short-term FY 2025 federal government funding continuing resolution (CR) extending the deadline to March 14. According to a CBO cost estimate, the CR rescinds $20.2 billion of amounts provided to the IRS under the Inflation Reduction Act. "CBO anticipates that rescinding those amounts would result in fewer enforcement actions by the IRS and thus in smaller revenue collections," the report states. CBO estimates the rescission will reduce revenues by $65.8 billion over 10 years.

For FY 2024, Congress provided $12.3 billion in annual funding, of which $5.4 billion was allocated to compliance activities separate from any Inflation Reduction Act compliance funding.

IRS enforcement

Several of the IRS enforcement initiatives could be affected by further cuts to the agency's enforcement funding. The extra funding provided by the Inflation Reduction Act has enabled the IRS to increase audits of large corporations, partnerships with more than $10 million in assets, and high-wealth individuals. The IRS collected more than $98 billion in enforcement revenue in fiscal year 2024.

As part of its multi-faceted approach, the IRS also has been able to expand its campaigns around corporate aircraft and the corporate alternative minimum tax. In addition, the IRS recently announced the recovery of $4.7 billion from recent initiatives that include investigations of wealthy individuals who have not paid taxes and the agency's pursuit of drug traffickers, cybercrime, and terrorist financing.

Last year, then-Treasury Deputy Secretary Wally Adeyemo said that further funding cuts would decrease the IRS's audit numbers for large corporations and high-income individuals by 8,000 across fiscal years 2025-2029 and increase the federal deficit by $140 billion over 10 years.

Direct File initiative

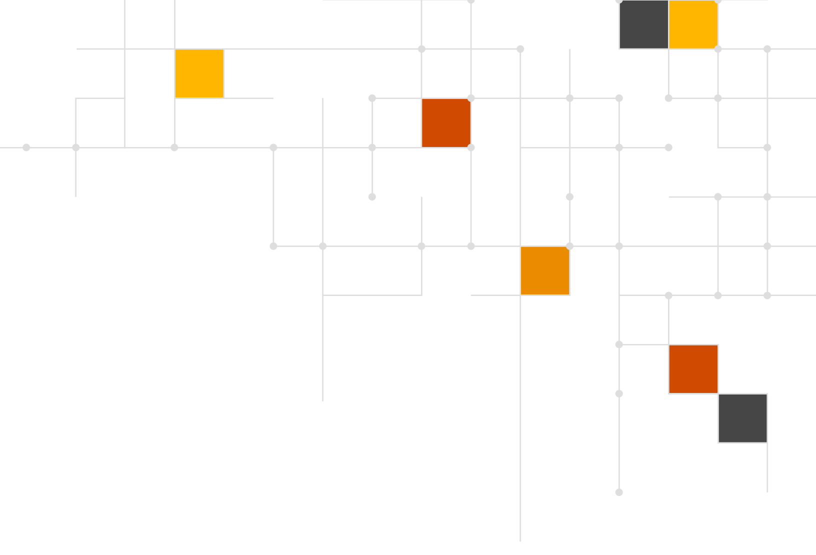
President Trump could direct the IRS to suspend the agency's Direct File tax return filing initiative that was piloted in 12 states with approximately 140,000 taxpayers in 2024. Treasury recently announced that the program would be available to over 30 million taxpayers in 24 states for the 2025 filing season.

Republican lawmakers, who have criticized Direct File as an overstep of IRS authority, sent a December 10 letter to President Trump, co-chairs of the Department of Government Efficiency (DOGE) advisory commission Elon Musk and Vivek Ramaswamy, and Treasury Secretary nominee Scott Bessent, calling on Trump to end Direct File on his first day in office, possibly through executive order.

The DOGE reportedly is exploring ways to mitigate taxpayer burden with respect to the preparation and filing of tax returns. One way the commission is considering simplifying the process is through the introduction of an app to help taxpayers file their tax returns directly with the IRS for free. It is not clear how the new app would interact with the mobile-friendly Direct File program.

IRS personnel

DOGE's plan to slash the federal workforce and the substantial cuts to IRS enforcement funding may have some agency employees preparing for a wave of early retirements. The increased funding the IRS received from the Inflation Reduction Act was partly meant to help expand IRS ranks to help keep up with the growing economy. A significant expansion of the IRS was underway, with the agency having a goal of reaching over 105,000 employees by 2025.



Global tax policy outlook

Status of the OECD/G20 Inclusive Framework's (IF) Two Pillar Project

Pillar Two

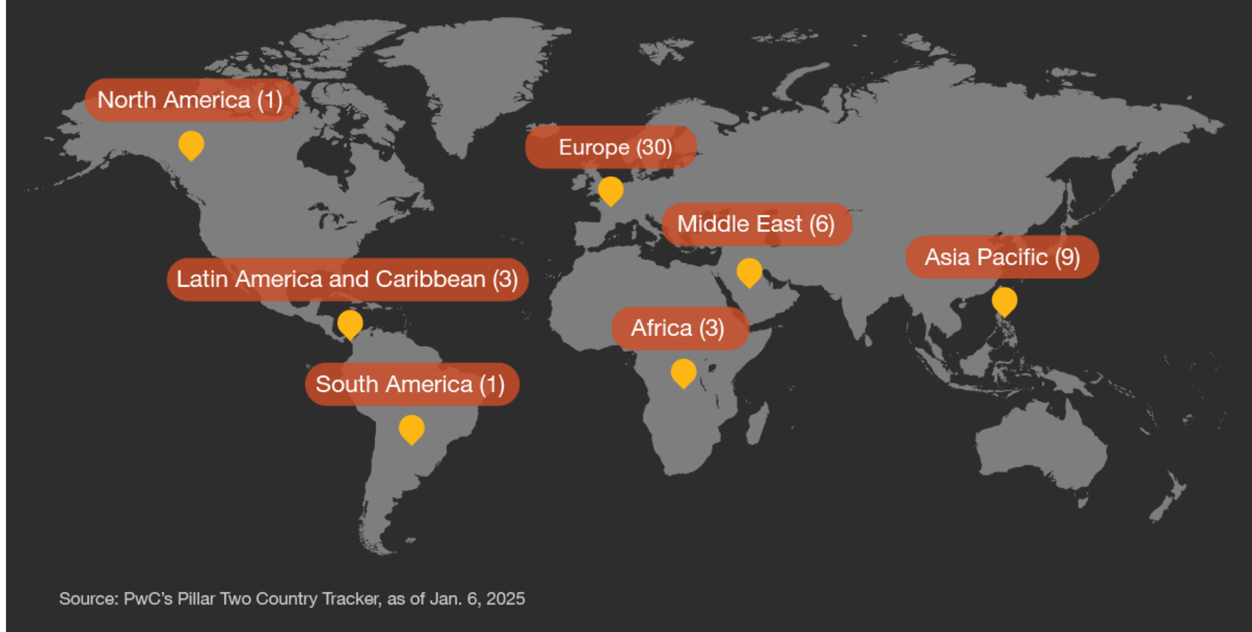
The OECD's Pillar Two global minimum tax framework has been adopted, at least in part, by numerous countries, aiming to establish a jurisdictional-level minimum tax system with a minimum effective tax rate (ETR) of 15%. Pillar Two applies to MNCs with global revenues exceeding EUR 750 million, while allowing jurisdictions to apply these rules to smaller domestic MNCs at their discretion. The OECD is expected to release additional implementation guidance in 2025.

The Pillar Two rules contemplate three different mechanisms for assessing tax on an MNC's income, and MNCs will have to comply with the filing requirements for each applicable rule:

- **Income Inclusion Rule (IIR):** The IIR generally imposes tax on the parent entity of an MNC group to the extent that the foreign subsidiaries of the MNC are taxed at a rate less than 15%, as determined for Pillar Two purposes (akin to a CFC-like tax on affiliated entities in other jurisdictions).
- **Qualified Domestic Minimum Top-up Tax (QDMTT):** The QDMTT is a tax that a country imposes on income earned within its own borders to ensure that such income is taxed at a rate of 15%.
- **Under Taxed Profits Rule (UTPR):** The UTPR was designed to act as a "backstop," allowing a country to impose additional tax on an entity if that entity has any affiliated entities in other jurisdictions that are taxed at less than the 15% Pillar Two rate. Certain US tax bills, discussed below, target the UTPR and similar measures.

Over 50 countries have either final or draft legislation to enact an IIR and/or QDMTT with effect from 2024 or 2025, as shown in Figure 11.

Figure 11: Status of global minimum tax implementation by jurisdictions with draft or final legislation



Source: PwC's Pillar Two Country Tracker, as of Jan. 6, 2025

The OECD is expected to release a list of countries that have transitional rule qualification status, which gives temporary recognition to a jurisdiction's legislation implementing the Pillar Two rules. That status allows countries to be considered compliant with the global minimum tax standards while undergoing a full review process, essentially providing a "grace period" for minor inconsistencies in their legislation before full qualification is confirmed.

Countries that have adopted a UTPR are expected to begin applying it in 2025. However, the UTPR has sparked concern over its potential to exacerbate not only tax, but also trade and political tensions, leading many countries to adopt a "wait and see" stance on its implementation. Legal criticisms and potential US retaliatory actions, such as those proposed during the previous 118th Congress in the Unfair Tax Prevention Act (H.R. 4695) and the Defending American Jobs and Investment Act (H.R. 3665), target the UTPR and similar measures. For example, H.R. 3665 proposed to increase income tax and withholding tax rates, initially by 5 percentage points, increasing up to 20 percentage points, that would apply to certain foreign citizens, certain foreign corporations, and certain foreign partnerships of any country that is listed in a Treasury Department report on extraterritorial and discriminatory taxes. The stepped-up tax rates would apply based on the amount of time a country is listed in the report.

Observation: Opposition from US lawmakers could embolden countries already hesitant about adopting a UTPR to delay implementation further. Within the EU, there are indications of reluctance to advance tax harmonization, coinciding with the EU's broader policy goal to shift away from overregulation to enhance competitiveness, which former European Central Bank chief Mario Draghi said was now more urgent than ever after Trump's election.

As the UTPR comes into effect in 2025, its application to US parent companies (and perhaps beyond) will face significant resistance from President Trump and the Republican majority in Congress. Action will be needed in the EU, where the Directive to implement Pillar Two is legally in effect, to deal with the UTPR's seeming incompatibility with overarching international law (i.e., tax treaties and other international agreements).

Observation: In the EU, tax proposals, including the Pillar Two minimum tax, require unanimous agreement from all Member States to be adopted and any subsequent changes also need unanimous approval. The EU Directive to implement Pillar Two generally mandates all Member States to apply the UTPR to financial years starting on or after December 31, 2024. However, US MNCs should be protected from the UTPR in 2025 with respect to their US income under the transitional UTPR safe harbor, which applies to any headquarter jurisdiction that has a 20% or greater headline corporate income tax rate (accounting for subnational taxes). This safe harbor is scheduled to expire in 2026.

One possibility is that countries could agree to extend or make permanent the transitional UTPR safe harbor, which might not require changes to the EU Directive given its references to OECD safe harbors. In that case, the US corporate income tax rate (including the effect of state and local corporate taxes) would have to stay at or above 20% to qualify.

Pillar Two registrations began as early as September 2024 (in Belgium). Filing of Pillar Two tax returns, including the GloBE Information Return (GIR) by each Constituent Entity or a designated Filing Entity, is required starting June 30, 2026 for calendar-year taxpayers. A QDMTT local tax return filing also may be needed in jurisdictions where a QDMTT is in place and may need to be filed before June 30, 2026.

Observation: Pillar Two represents the most significant corporate tax reform in a generation and will fundamentally change how large businesses calculate and pay tax internationally. Pillar Two's widespread adoption, including the anticipated divergence in local rules, poses additional complexities that cannot be overstated. These historic changes will affect effective tax rates, significantly increase compliance obligations, impact legal structures, change deal values, and force MNCs to source data that might be difficult to obtain. While potentially meaningful changes to the Pillar Two framework may occur as a result of pressure from the Trump Administration or other factors, the clock cannot be turned back completely as other countries continue to move forward. The evolving political landscape over the next several months will be a critical factor in shaping the future of these tax policies.

Pillar One

Amount A: The OECD's Pillar One initiative, specifically Amount A, represents a significant shift in international tax policy. It introduces a formulaic approach to reallocating a portion of the global residual profits of MNCs to market jurisdictions, where their consumers reside, rather than where the businesses physically operate. Amount A targets MNCs with over EUR 20 billion in global revenues, equivalent to approximately USD 20.5 billion as of January 3, 2025, and a profit margin greater than 10% (i.e., profit before tax divided by revenue). It excludes companies in the extractive and financial services sectors.

In October 2023, the OECD released a Multilateral Convention (MLC) to facilitate the implementation of Amount A. As of the end of 2024, the MLC draft was not yet open for signature due to unresolved issues, although it is considered "stable" by the OECD. Pillar One's main delay deals with Amount B (discussed below) and its interdependence with Amount A, and ultimately a disagreement between the United States and India over how binding Amount B should be.

For the MLC to enter into force, it needs to be ratified by at least 30 jurisdictions, including the headquarters' jurisdictions of at least 60% of MNCs currently expected to be within Amount A's scope. Crucially, the 60% threshold cannot be reached without the United States' participation.

Observation: The Trump Administration will not sign the MLC. Moreover, achieving the necessary 67 Senate votes for ratification in the United States presents a likely insurmountable challenge due to procedural hurdles and a lack of bipartisan support.

Amount B: In February 2024, the OECD released a report on Amount B of Pillar One, now referred to as the 'simplified and streamlined approach,' which attempts to simplify the transfer pricing of certain baseline wholesale marketing and distribution activities by providing agreed returns to the source country, as laid out in a "pricing matrix" for such activities. The scope of the guidance is limited to wholesale distribution of tangible goods and does not include services (including digital services) or commodities. This approach has been integrated into the OECD Transfer Pricing Guidelines as an annex to Chapter IV. Amount B is optional and can be implemented for fiscal years starting on or after January 1, 2025. Countries adopting Amount B have two choices: they can either make the framework binding on all applicable taxpayers or allow it as an elective safe harbor for taxpayers who meet specific criteria.

The implementation of Amount B is supported by a political commitment from all IF members (subject to their domestic legislations and administrative practices) to take all reasonable steps to relieve potential double taxation that may arise from the application of Amount B by a "Covered Jurisdiction" (previously referred to as low-capacity jurisdictions) where there is a bilateral tax treaty in effect. Additional guidance on Amount B — including the definition of Covered Jurisdiction for the IF's political commitment on Amount B — was published in June 2024. The guidance lists 66 countries, including Argentina, Brazil, Costa Rica, Mexico, and South Africa.

Observation: Being listed as a Covered Jurisdiction does not mean that the country is required to adopt the Amount B framework, but per the IF political commitment, that country will respect the transfer pricing outcome determined under Amount B to in-scope transactions where such approach is applied by Covered Jurisdictions. The number of countries that adopt Amount B, and how they do so, could depend on the outcome of the Pillar One MLC. It remains crucial for businesses operating with limited risk distributors, commissionaires, or sales agents to closely monitor these developments and assess their implications for their current transfer pricing policies.

The OECD is expected to publish a list of countries that have chosen to adopt Amount B. This list is expected to indicate each country's adoption methodology — which could be either as a taxpayer safe harbor or the prescribed method in the particular country. Several countries, including Ireland, Spain, Australia, and New Zealand, have said they will not adopt Amount B outside of the political commitment concerning Covered Jurisdictions.

United States to propose transfer pricing regulations adopting Pillar One's Amount B

On December 18, 2024, Treasury and the IRS issued guidance (Notice 2025-04) announcing their intention to issue proposed transfer pricing regulations adopting the simplified and streamlined approach (SSA) (i.e., Amount B) of Pillar One as a taxpayer-elective safe harbor.

According to the Notice, the proposed regulations will “provide a new method for pricing certain controlled transactions involving baseline marketing and distribution activities” as described in the OECD’s February 2024 Report on Amount B. The Notice states that Treasury and the IRS expect that the proposed regulations will not substantively diverge from any aspect of the OECD Report and will implement the substance of the OECD Report in its entirety.

Observation: Taxpayers engaged in distribution activities that could fall within the scope of the SSA should evaluate the potential impact of the SSA on their existing transfer pricing policies. It is important to determine whether electing the SSA would be beneficial and to identify any necessary steps to qualify for its application. Additionally, taxpayers and organizations should consider participating in the public comment process, with written comments requested by March 7, 2025, to help shape the final regulations.

Renewed focus on Digital Service Taxes and other relevant unilateral measures

The OECD's negotiations on Pillar One, particularly Amount A, were largely driven by the goal of curbing the spread of DSTs and similar unilateral measures. The draft MLC for implementing Amount A mandates the abolition of existing DSTs and similar measures for all companies and includes a commitment from countries not to introduce such measures in the future.

Annex A of the MLC lists nine specific measures that must be removed, representing actions in eight countries, including two in India, one in Tunisia, and six in Europe, where DSTs initially gained traction (Austria, France, Italy, Spain, Turkey, and the United Kingdom). Additionally, the MLC requires countries to avoid applying Significant Economic Presence (SEP) criteria or similar nexus rules to MNCs within the scope of Amount A, a concept supported by some developing and emerging economies. The MLC offers countries the choice either to adopt Amount A, benefiting from the reallocation of tax revenues, or to continue with or introduce new domestic DSTs.

The IF conditionally agreed to extend a moratorium on new DSTs and similar measures beyond December 31, 2023, contingent upon a critical mass of countries, including the United States, signing the MLC in 2023. Although the OECD aimed for the MLC to be open for signature in 2023, the IF extended the timeline to finalize the MLC text by March 2024, with a signing ceremony anticipated by June 2024. This extension was accompanied by efforts to prolong the moratorium on DSTs and similar measures that was set to expire at the end of 2023. The US Treasury's 2021 "Unilateral Measures Compromise" agreements with Austria, France, Italy, Spain, the United Kingdom, Turkey, and India were extended to the end of June 2024, but all these agreements have expired. It remains uncertain if they will be renewed given the current state of affairs.

DSTs have found support in certain regions. In Africa, a model for drafting DST laws has been developed, and the African Tax Administration Forum (ATAF) has encouraged its members to consider such measures until a global resolution is achieved. In Latin America, there have been efforts to form a regional consensus on the reallocation of taxing rights, potentially leading to the emergence of different unilateral or multilateral measures.

Observation: Unless further agreements are made, MNCs in 2025 should anticipate the proliferation of new unilateral measures, including DSTs, expanded withholding taxes on digital services, equalization levies, non-traditional nexus-based levies (e.g., SEPs), and other similar measures that are expected to fall primarily on US businesses. A multilateral DST also could be proposed at the EU level.

Other global tax policy developments

The United Nations asserts a greater role in global tax policy

On December 24, 2024, the UN General Assembly approved by majority vote (119 countries in favor, nine against, and 43 abstaining) the Resolution that adopts the terms of reference (ToR) for negotiating a UN Framework Convention on International Tax Cooperation (Framework Convention). The Resolution calls for establishing an "open-ended intergovernmental negotiating committee" for drafting the Framework Convention and two early protocols (simultaneously). The ToR commits negotiators to two sub-agreements, called protocols, with one focused on "cross-border services in an increasingly digitalized and globalized economy" with the other still to be decided.

The timeline and locations for the negotiations are as follows according to the Resolution:

- February 3-6, 2025 in New York, to address organizational matters and decide on the subject of the second early protocol (to be drawn from a list that includes the taxation of the digitalized economy; tax-related illicit financial flows; preventing and resolving tax disputes; and tax evasion and avoidance by high-net-worth individuals);
- Early May 2025 in New York for the first substantive session;
- August 4-15, 2025 in New York, for the second substantive session; and
- November 10-21, 2025 in Nairobi, for the third substantive session.

The Bureau of the intergovernmental negotiating committee will have a Chair, 18 Vice-Chairs and a Rapporteur, to be elected based on equitable geographical representation. International organizations, civil society, and other relevant stakeholders are encouraged to participate in the process. The text of the multilateral treaty and the two early protocols should be delivered to the General Assembly during the first quarter of its 82nd session, which is expected to begin in September 2027, according to the ToR.

Observation: The United States, the EU, the UK, and Japan (among other developed nations) have raised concerns that the UN international tax cooperation effort so far has not been based on consensus decision-making. In its explanation of vote, the EU threatened it "may have to choose to disengage" from future negotiations if simple majority decision-making continues to be utilized. While this opposition will not prevent the process from moving forward, it suggests enduring or effective outcomes may be difficult to achieve.

EU developments expected to affect MNCs

Poland takes over the Presidency of the Council of the EU from Hungary in the first half of 2025, followed by Denmark in the second half of 2025. The Polish government's overarching priorities include security (external and internal, energy, economic, food and climate, health and information) and economic competitiveness. In the field of taxation, EU competitiveness has been highlighted as a key objective leading up to Poland's presidency. Commission President Ursula von der Leyen, who was re-confirmed in July 2024 for another mandate, has promised to reduce corporate reporting obligations by 25% across the board, and 35% for small businesses.

Observation: Poland will take over the EU's rotating presidency at a moment of instability within and outside of the EU, coinciding with a new set of Commissioners, the three-year anniversary of Russia's invasion of Ukraine, political turmoil in Germany and France, and President Trump's inauguration.

In November 2024, the EU Parliament approved (with a very thin majority) the new College of Commissioners for 2024-2029. The Commissioners assumed office on December 1, 2024. Tax is a significant part of the files entrusted to Commissioners Wopke Hoekstra (Commissioner for Climate, Net Zero and Clean Growth) and Valdis Dombrovskis (Commissioner for Economy and Productivity; Implementation and Simplification) as well as Teresa Ribera (Executive Vice President for a Clean, Just and Competitive Transition). Dombrovskis during his hearing mentioned that simplification (decluttering) does not mean de-regulation. Ribera will have to work closely with Hoekstra to ensure that taxation will foster a just transition, and the European Commission is expected to come up with a proposal on this matter in the near future.

Observation: While there has been a lot of emphasis on the EU policy goal to shift away from overregulation (i.e., "decluttering") to enhance competitiveness, the lack of a single Commissioner owning the tax agenda could complicate that effort.

The following is an overview of the state of play of some key initiatives under negotiation in the area of EU taxation. As noted above, under EU rules, EU countries must agree to new tax laws unanimously.

- **CSRD:** In November 2022, the EU formally adopted the Corporate Sustainability Reporting Directive (CSRD), which requires companies operating in the EU to publicly disclose and report on Environmental, Social, and Corporate Governance (ESG) issues. The rules will start applying between 2024 and 2028, depending on the size of the company. The Commission is expected to present an Omnibus proposal in February 2025 in which CSRD, the Corporate Sustainability Due Diligence Directive (CSDDD or CS3D) and the EU Taxonomy Regulation are integrated.

- **EU Foreign Subsidies Regulation:** As of October 12, 2023, companies had to notify and seek approval from the EU Commission if a non-EU government provides broadly defined "financial contributions" to a business, such as a grant, export subsidy, or tax credit, that could provide an unfair advantage against EU companies. The Commission can order a wide range of "redressive measures," including repayment of the subsidy, granting of licenses to IP, or prohibiting an M&A transaction or participation in a public procurement process if it believes the foreign subsidies have a distortive effect in the EU (and EEA). A number of cases were taken by the Commission in 2024 following both notifications by impacted groups and ex-officio investigations taken by the Commission, with the first results of those cases recently made public. Further clarification and enforcement activity is expected in 2025.

- **Public CbCR:** The EU's public CbCR directive, published in December 2021, is being transposed into individual Member States' legislation. The latest date for this to apply is for accounting periods beginning on or after June 22, 2024. The EU public CbCR Directive would apply to both EU and non-EU based MNCs operating through a branch or subsidiary with total consolidated revenue of more than EUR 750 million in each of the last two consecutive financial years. There is overall uncertainty regarding what information is "commercially sensitive" and how companies can avail themselves of deferred reporting. A common template for reporting by EU-based MNCs was published in December 2024.

- **Administrative Cooperation (DAC) 8:** The DAC8 Directive was adopted in October 2023, amending the EU rules on administrative cooperation in the area of taxation. The amendments primarily pertain to the reporting and automatic exchange of information on certain revenues from crypto asset transactions and the provision of advance tax rulings for high-net-worth individuals. Member States are required to transpose DAC8 into national law by December 31, 2025, with most provisions becoming effective on January 1, 2026 at the latest.

- **DAC9:** In October 2024, the EU Commission announced a new proposal (DAC9) to amend DAC. The DAC9 proposal transposes the OECD's July 2023 GloBE Information Return (GIR) into EU law by making it the Top-up Tax Information Return (TTIR) as required by Article 44 of the EU minimum tax Directive (Pillar Two Directive). It also proposes an EU framework to facilitate the exchange of TTIR information between Member States. If adopted by the EU Council, DAC9 would have to be implemented into national law by December 31, 2025; i.e., six months prior to the first filing deadline of the TTIR for most groups in scope of Pillar Two rules. DAC9 is scheduled for discussion at the ECOFIN meeting in April 2025.

- **FASTER:** On December 10, 2024, the EU Council approved the Faster and Safer Relief of Excess Withholding Taxes (FASTER) Directive. The initiative is designed to encourage investment in the EU market by making withholding tax procedures in the EU more efficient and secure for investors, financial intermediaries, and Member State tax administrations. Member States will need to adopt and publish the necessary laws, regulations, and administrative provisions by December 31, 2028, and will be required to apply the provisions of the Directive from January 1, 2030.
- **Carbon Border Adjustment Mechanism:** The Carbon Border Adjustment Mechanism (CBAM) was formally adopted by the EU Council in 2023, with the transitional phase's entry into force on October 1, 2023, for certain products. The CBAM is aimed at preventing carbon leakage by EU-based companies that relocate their production outside the EU to avoid the EU's climate regulation costs. Until the end of 2025, the CBAM only entails a reporting obligation. The levying of import charges will only commence in 2026 and will be introduced gradually over a period of nine years.
- **VAT in the Digital Age (ViDA):** The Council of the EU announced in November 2024 that agreement was reached on the ViDA package. This is a significant reform package introducing e-invoicing and e-reporting changes. The EU Parliament must be consulted on the package directive, after which it can be formally adopted by the Council and published in the Official Journal of the EU.

US tax treaty developments

Taiwan

The Senate last August blocked a House-passed bill (H.R. 7024) that included provisions to provide treaty-like benefits aimed at relieving double taxation for businesses engaged in cross-border activities between the United States and Taiwan. The legislation would have made benefits available to Taiwan corporate tax residents other than "qualified residents" of Taiwan provided that the relevant income satisfied an active trade or business test. The legislation also included provisions to authorize the negotiation of a US-Taiwan tax agreement providing double taxation relief.

In October 2024, Treasury and the Taiwanese Ministry of Finance separately announced that the United States and Taiwan, under the guidance of the American Institute in Taiwan and the Taipei Economic and Cultural Representative Office in the United States, would begin negotiations on a comprehensive agreement to address double taxation issues. The tax agreement is expected to be based on the US Model Income Tax Convention. Treasury indicated it will consult Congressional committees during the negotiation process and work with Congress on legislation to approve a final agreement and implement the agreement through the Internal Revenue Code.

The House in January approved a new bill (H.R. 33) to provide double taxation relief for businesses engaged in cross-border activities between the United States and Taiwan. While the House action indicates ongoing bipartisan support for addressing this issue, the timing of Senate action is uncertain.

Russia

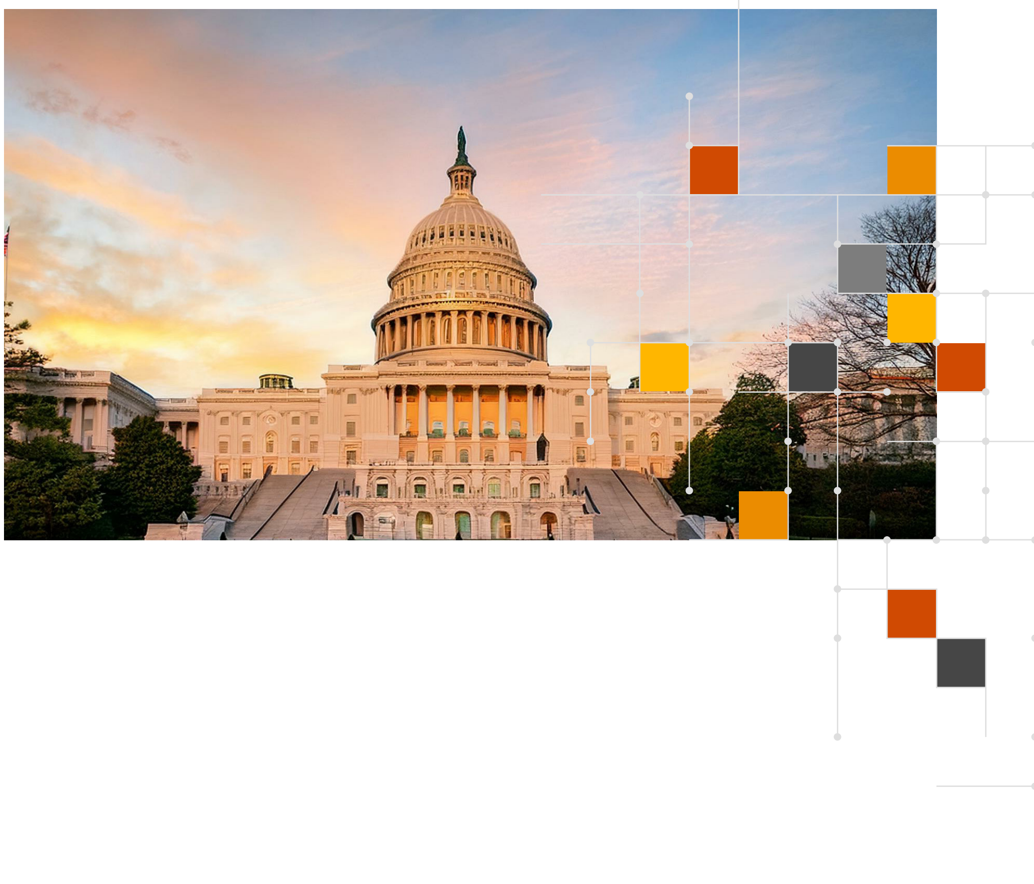
The tax treaty between the United States and Russia was partially suspended for taxes withheld at source and for other taxes, effective August 16, 2024. The suspension will continue until otherwise decided by the two governments.

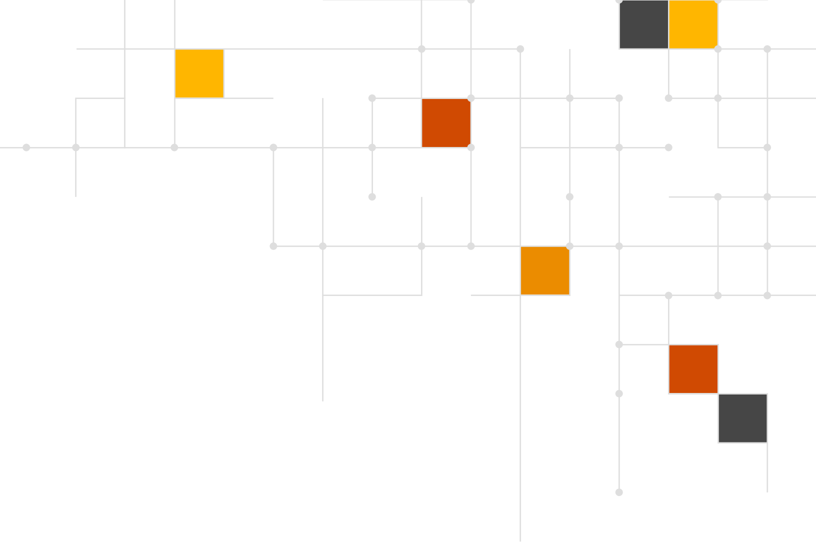
Belarus

The United States provided formal notice to the Republic of Belarus on December 17, 2024, to confirm partial suspension of the 1973 tax convention between the United States and the Union of Soviet Socialist Republics (USSR) as it relates to Belarus. The suspension is effective December 17, 2024, until December 31, 2026, or earlier if mutually determined by the two governments.

Other treaty developments

The United States continues to negotiate new tax treaties with various countries. Negotiations with Switzerland are substantially complete; however, the timing of signing and ratification is uncertain. Other treaties that have been signed by the United States but not yet ratified by the Senate may require modifications to reflect TCJA international provisions.





Trade policy outlook

Industry stakeholders are anticipating significant cost increases if the Trump administration implements the tariff increases that have been announced by President Trump over the past several months.

Actions to implement President Trump's trade policy agenda that features potential tariff increases could involve a mix of executive and legislative actions.

Observation: Several existing tariff increases implemented by presidential action are subject to legal challenges, and it is expected that any future impositions of tariffs could face similar obstacles.

Key administration trade policy officials

President Trump has assembled a team of key players to assist with trade and tariff efforts.

- **Jamieson Greer** has been nominated to be the United States Trade Representative (USTR). Greer served as Chief of Staff to the USTR during Trump's first term.
- **Howard Lutnick** has been nominated to lead the Commerce Department, which plays a key role in the execution of US trade laws and the administration of tariff policies.
- **Peter Navarro**, former Director of the White House Office of Trade and Manufacturing Policy during President Trump's first term, has been chosen to serve as White House Senior Counselor for Trade and Manufacturing.

Industry impact

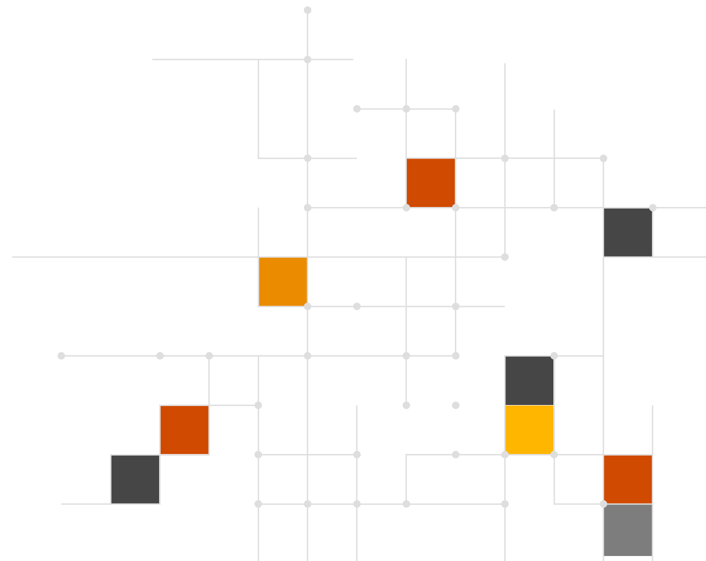
Industry stakeholders are anticipating significant cost increases if the Trump administration implements the tariff increases that have been announced by President Trump over the past several months, particularly in sectors heavily reliant on cross-border manufacturing and sourcing.

To help understand the impact, PwC conducted a benchmarking analysis that utilized 12 months (October 2023 to October 2024) of US Census data along with President Trump's announced pre-inauguration tariffs (up to 60% for China, 25% for Mexico, 25% for Canada, and 20% for all other imports in the rest of the world (ROW) across all dutiable and non-dutiable goods). The analysis involved 107 industries and imports from 233 countries into the United States. The results are illustrated in the table below.

Figure 12: The potential impact of Trump's tariffs on current US annual dutiable/non-dutiable imports

	Current State		Potential Trump Tariff Impact				
Type of Goods	Import Value	Current Tariff	Potential China	Potential Mexico	Potential Canada	Potential ROW	Potential Total
Dutiable	**$1T**	$81b	$172b	$13b	$24b	$124b	$334b
Non-Dutiable/ FTA	**$2.3T**	$0	$100b	$119b	$82b	$261b	$562b
Total	**$3.3T**	$81b	$272b	$132b	$106b	$385b	$896b

Source: PwC Tariff Modeling Analysis relying on US Census Bureau, "Monthly U.S. Imports by North American Industry Classification System (NAICS) Code," as of December 17, 2024. Amounts refer to annual imports from October 2023 to October 2024.



A total of $3.3 trillion in import value of goods enter the United States on an annual basis. Of that, $2.3 trillion is currently being imported under the terms of a Free-Trade Agreement (FTA) or free of duties based on current regulations; therefore, US companies are not paying duty on that value. US companies are paying duties on the remaining $1.0 trillion of imported goods, which results in duties of $81 billion for a 12-month period.

Based on statements by President Trump, the new administration may take the position that FTAs are no longer applicable, and duties would be assessed on the full import value of all goods. This means going forward the full US import value of $3.3 trillion (including the $2.3 trillion that is currently duty-free under an FTA) would be assessed duties and fees. This would bring in a multitude of companies being subject to tariffs.

Based on the same data set, PwC's benchmarking analysis layered on President Trump's potential tariffs on existing dutiable goods and non-dutiable goods. The estimated annual tariff amount would increase to $896 billion (from $81 billion) and $334 billion would be from current dutiable goods and non-dutiable goods would go from **zero** to $562 billion. The non-dutiable goods jump could have the largest impact to US multinationals in 2025 that use the FTA programs in their operating models.

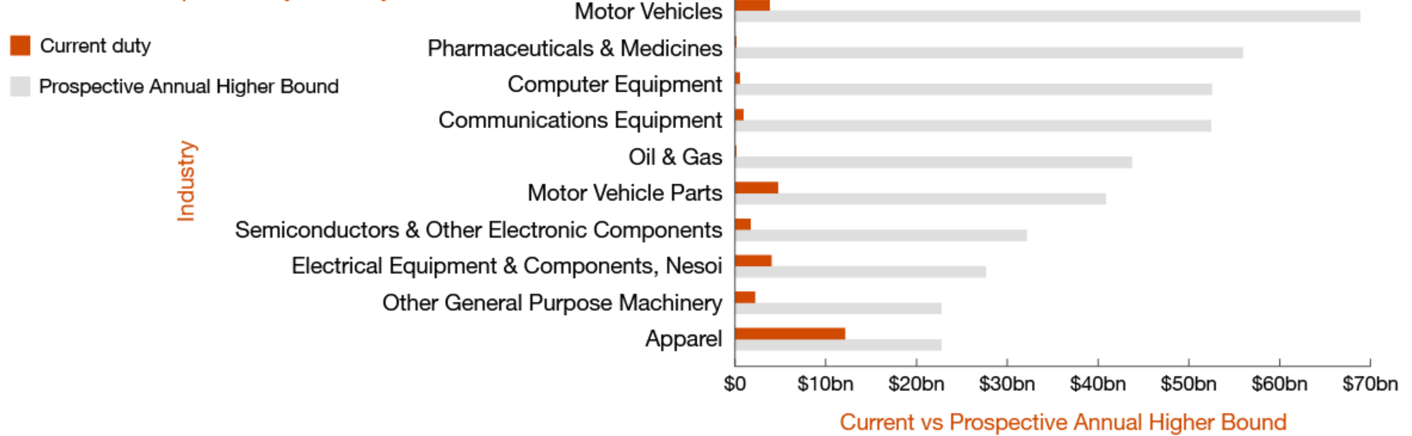
For US importers that depend on products from China, tariffs on goods would increase to approximately $272 billion a year. When compared to the $81 billion in current-state tariffs that are predominantly China-origin good tariffs, this would be a $191 billion increase in new tariffs on China goods.

For goods coming from Mexico, which is the United States' largest trading partner, the proposed tariff increase would have the biggest impact to US multinationals that use imports from Mexico, with a potential increase of $132 billion in annual tariffs. This is assuming that tariffs would be applied to all tangible products coming from Mexico to the United States regardless of tax structure (e.g., if the company is a Maquiladora, toll manufacturer, or contract manufacturer). Manufacturers of motor vehicles and parts, computer and electrical parts, and machinery as well as agricultural importers of fruits, vegetables, grains, and sugar could see the largest increase in costs.

For goods coming from Canada, the United States' second largest trade partner, the proposed tariffs would result in an increase in annual tariffs of more than $106 billion. The biggest industries impacted would be oil and gas products, aluminum processing goods, motor vehicles and parts, and some operating in the food product industry.

Lastly, and with the widest range of impact, are the goods imported from the rest of the world. These are goods that previously were non-dutiable or had a lower tariff rate in comparison to the 20% potential rate. Affected industries should be prepared as this would be a new cost to be considered as part of business operating models. These new tariffs could impact industries that may have relocated operations outside of China to address the previous tariff increases, as well as pharmaceuticals that were exempt.

Figure 13: Greatest dollar increase in prospective tariffs — Top 10 industries

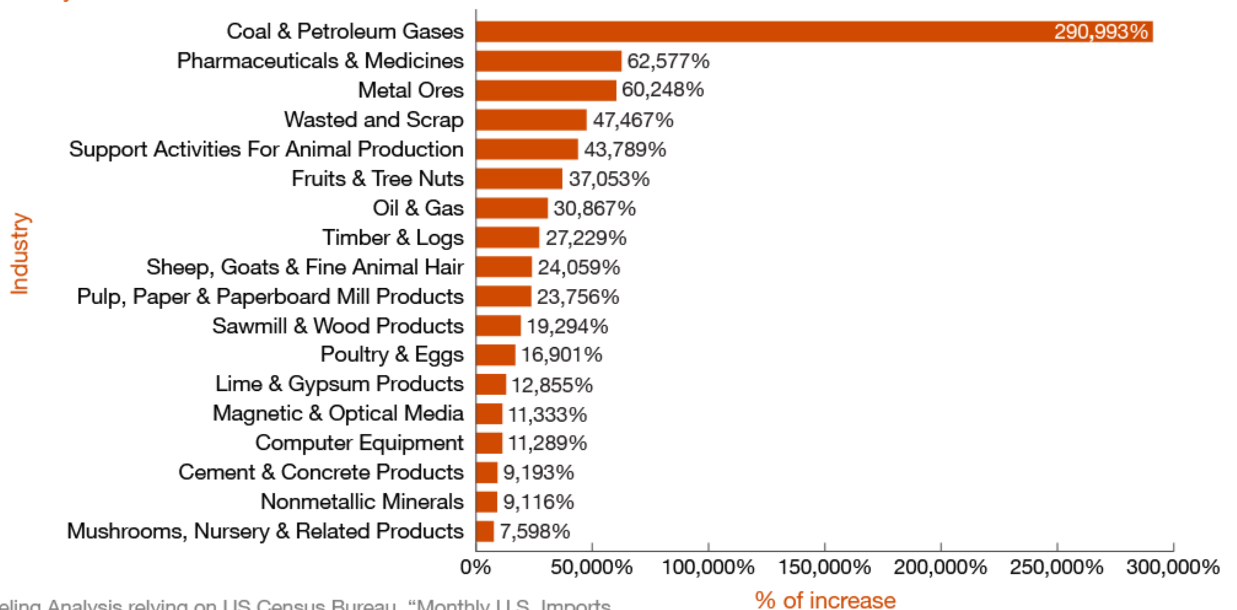


Source: PwC Tariff Modeling Analysis relying on US Census Bureau, "Monthly U.S. Imports by North American Industry Classification System (NAICS) Code," as of December 17, 2024.

To analyze the current vs. proposed tariff state, below is a summary of the prospective annual impact for the top industries with the largest incremental increase of potential tariffs in comparison to the current duty rates.

Industries such as pharmaceuticals, computer and communication equipment, and oil and gas are currently experiencing low duty rates associated with their high import value. Therefore, the potential for increased duty is substantial if non-dutiable goods are included in the import value base and subject to all proposed tariffs. For example, the level of tariffs paid by the pharmaceuticals and medicines industry group is projected to jump from approximately $90 million to over $56 billion a year. In addition, the automotive and technology sectors currently pay duties, but the increase from nearly $4 billion to over $68 billion would make them some of the hardest hit industries.

Figure 14: Greatest percentage increase in prospective tariffs — Top 18 industries



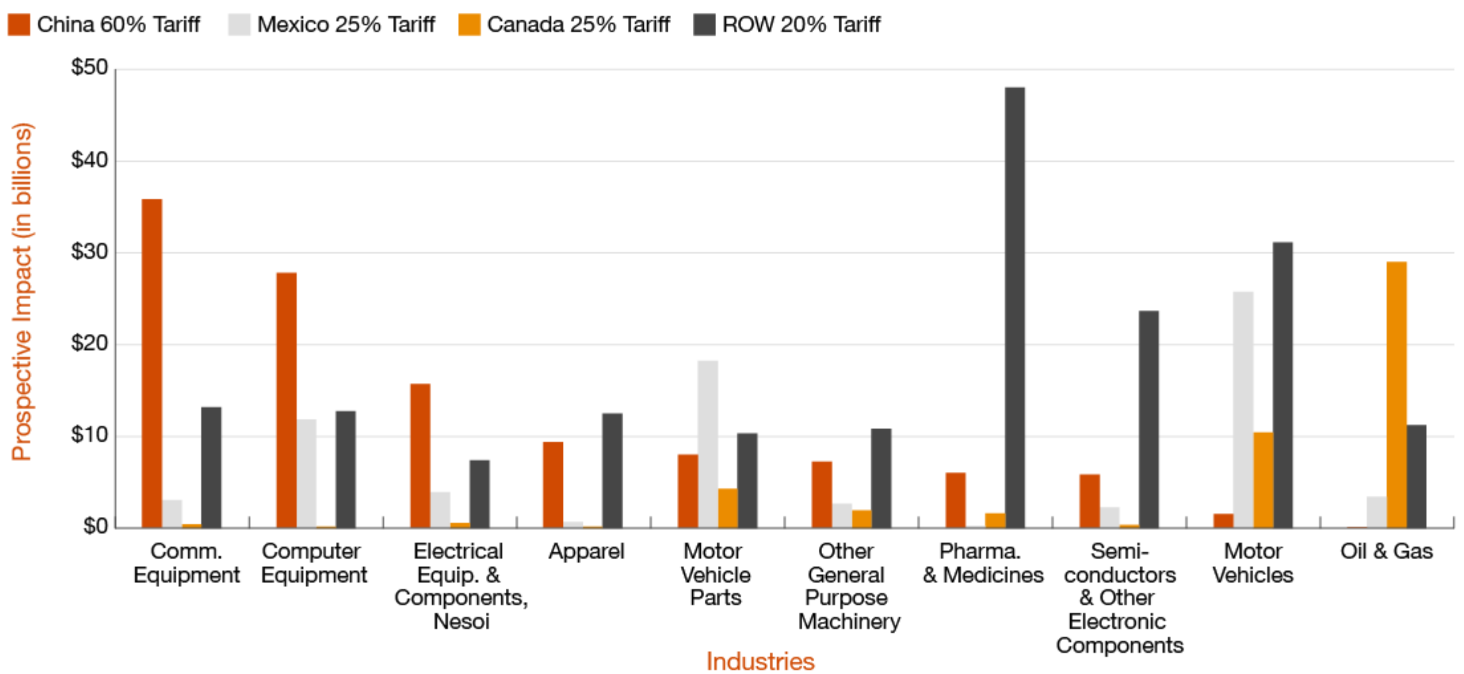
Source: PwC Tariff Modeling Analysis relying on US Census Bureau, "Monthly U.S. Imports by North American Industry Classification System (NAICS) Code," as of December 17, 2024.

This same data set looks very different when focusing on the significant percentage increases by industry, as shown above in Figure 14.

Industries that could have the largest percentage impact are those that were historically zero-tariffed (i.e., part of the non-dutiable goods category). Tariff impacts for this group of industries is forecasted to jump from zero to $562 billion.

From a country perspective, this would have a big impact to any company that utilizes Mexico, Canada, or other imports (other than China) since goods could see a punitive increase from zero to 20% in tariffs. One industry sector that would be heavily impacted is the "coal and petroleum gases" category, which largely is imported into the United States from Canada.

Figure 15: Top 10 industries — impact by potential rate per country



Source: PwC December 2024 Tariff Modeling Analysis using US Census Bureau, "Monthly U.S. Imports by North American Industry Classification System (NAICS) Code," as of December 17, 2024.

Figure 15 shows the largest impacted industries based on the tariff rate per country. The supply chain of the industry impacts which potential policy is relevant for that industry.

The proposed tariffs are set to create significant challenges across industries:

- **Technology and electrical equipment:** Companies importing semiconductors and electronic components from China are preparing for significant impact.
- **Pharmaceuticals and life sciences (classified as chemicals per Census database):** Previously exempt from most tariffs, companies in these industries could have the largest exposure if the ROW rates are enacted.
- **Transportation and automotive:** Manufacturers reliant on vehicles imported from Mexico and Canada would face cost increases due to the 25% rate from those countries, plus the proposed 100% to 200% tariffs on cars from Mexico.

- **Retail:** The apparel and consumer goods sectors anticipate higher costs, which may lead to increased prices and softened demand.
- **Oil and gas:** Companies integrated with Canada's energy and utility sectors should anticipate higher costs on goods that were previously free from tariffs.

Observation: Each multinational corporation should evaluate its pre- and post-impact of the potential tariffs on their annual operating profit using data driven insights to help drive go-forward options.

Business model impact

The post-2024 election period, marked by renewed tariff increase proposals and the looming threat of retaliatory measures, already has created a confluence of challenges across tax, transfer pricing, supply chain, and investment strategies. The introduction of new tariffs or the escalation of existing ones could significantly alter the cost structures for multinational enterprises, prompting reassessments of inter-company pricing policies, customs value methods, origin determinations, and more to ensure compliance with evolving regulations. For businesses, the heightened uncertainty underscores the need for integrated strategies that align tax planning, transfer pricing policies, and investment decisions with a forward-looking approach to supply chain resilience in an era of intensified trade policy volatility.

Observation: As a result of the anticipated disruptions to global commerce and trade, costs associated with production, regulatory, and tax compliance will likely rise and potentially multiply for many companies. Companies reliant on global sourcing should proactively adapt to this evolving trade environment to reduce financial and operational risk across the value chain. This will necessitate a multi-pronged approach to adaptation across the supply chain, trade and customs, and tax departments.

Trade and customs: Duty mitigation programs offer critical opportunities to offset cost increases. Strategies such as duty drawback allow businesses to recover duties when goods are exported from the United States. Other duty mitigation strategies include "first sale for export," which can reduce the dutiable value of goods, duty deferral programs such as foreign trade zones, and temporary importation provisions. If President Trump's proposed tariff measures provide for an exclusion request mechanism, it will be imperative for interested parties to participate in those proceedings. Companies should integrate these programs into broader trade planning to increase benefits.

Supply chain logistics: Businesses should assess the financial exposure posed by the proposed tariffs through comprehensive modeling. Scenario analysis can identify vulnerabilities and evaluate potential retaliatory measures by trade partners. By reassessing sourcing and manufacturing strategies, companies can build resilient supply chains capable of weathering disruptions.

Tax and valuation considerations: Supply chain disruptions stemming from trade tensions may necessitate reconfigurations, including the relocation of manufacturing operations or changes to sourcing profiles, to reduce risk and preserve operational continuity. These shifts intersect with tax implications, as cross-border restructuring and profit allocation adjustments may trigger complex compliance and tax efficiency considerations. Companies should consider revisiting their customs valuation strategies to identify opportunities to address these potential changes.

The transfer pricing (TP) impact of the proposed tariffs should be calculated to see how the results compare to the transfer pricing comparables used in TP documentation. TP adjustments also can be explored as a potential mitigation strategy but must be reviewed carefully from both a TP and customs perspective to assess compliance. Additionally, while it remains uncertain, businesses should monitor for the possibility of an exclusion process like those made available in prior years.

Observation: Aligning supply chain, tax, customs, and financial strategies is essential to reduce risks and avoid unexpected costs. Effective management of inter-company pricing can help address the conflicting priorities of tax authorities and customs agencies. A coordinated approach can help businesses navigate these complexities while maintaining stability and achieving an effective governance and compliance framework.

North American regional trade impact

The evolving trade relationship between the United States and its North American partners is expected to be a critical area of focus in early 2025. Developments in trade agreements and the implementation of global tariffs by all parties are creating a dynamic environment, positioning the region as a significant area of interest for trade policy and economic strategy.

The United States-Mexico-Canada Agreement (USMCA) continues to be a focal point for regional trade, but recent developments have added new layers of complexity. Under the USMCA review clause, the United States, Mexico, and Canada must confirm in writing by July 1, 2026, whether they intend to continue the agreement. If any party opts not to renew, it will initiate a process that could leave the future of the USMCA uncertain for years. During his 2024 campaign, President Trump signaled his intention to invoke the six-year renegotiation provision.

Observation: Challenges to the partnership with Canada and Mexico were already evident, even before the 2024 election. With the Biden administration targeting Chinese-origin steel and aluminum transiting both Canada and Mexico, the longevity of the USMCA was already in question. In 2024, both Canada and Mexico took measures to protect their own regional trade interests, which will complicate supply chains for companies leveraging operating model structures across these territories.

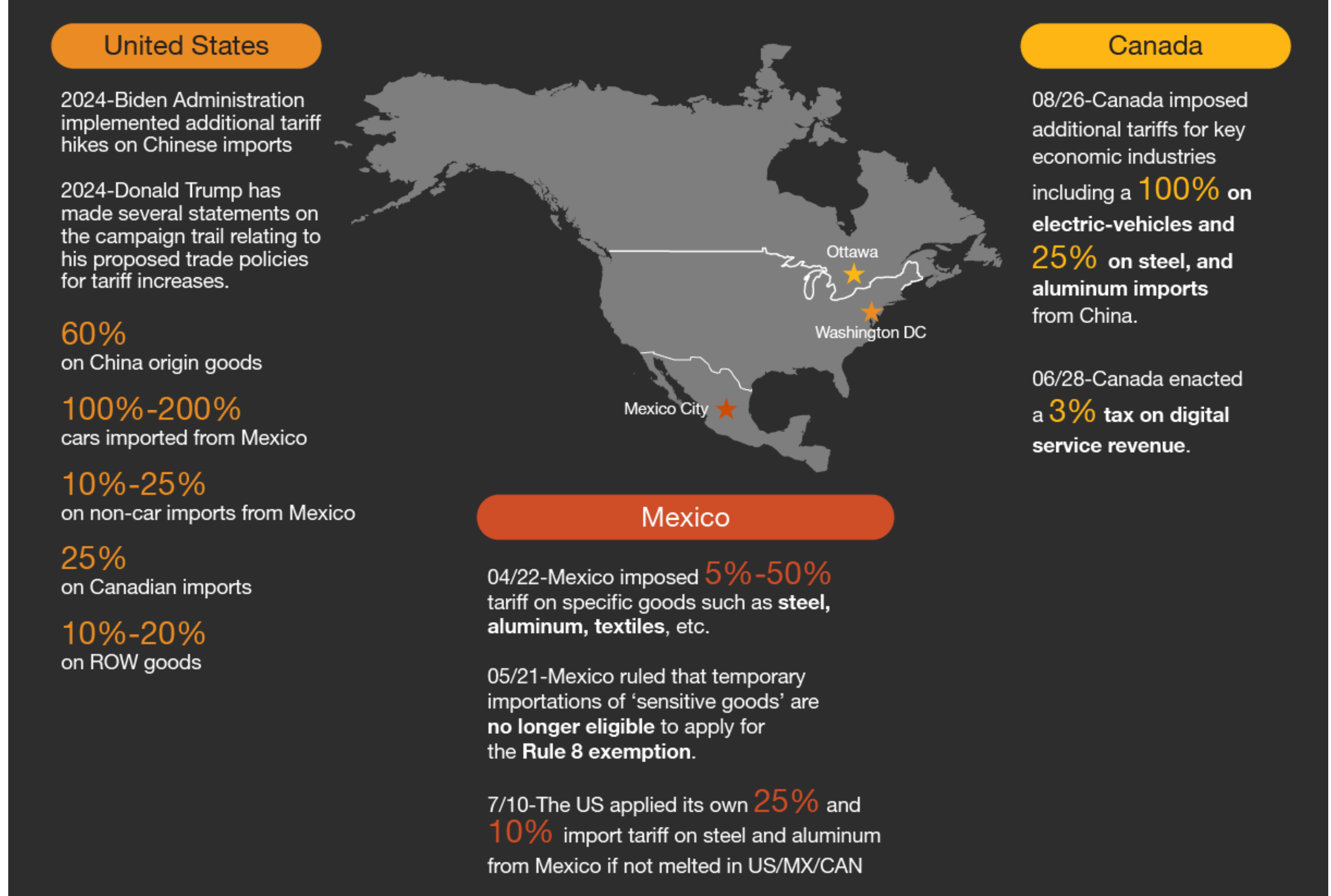
In Mexico, tariffs ranging from 5% to 50% on sensitive products have significantly increased costs for companies importing goods into Mexico from non-free-trade-agreement countries. In addition, changes to Maquiladora rules have curtailed the preferential treatment that previously allowed temporary imports of certain “sensitive” products to be exempted from duties. Many US manufacturing companies operating in Mexico took advantage of those rules.

Meanwhile, Canada imposed a digital services tax. As a result, the USTR requested a dispute settlement consultation with Canada under USMCA, stating that this DST targets revenues from online marketplaces, targeted advertising, social media platforms, and user data. Historically, the USTR has imposed retaliatory tariffs on select products imported from other countries that have implemented DSTs like Canada's.

In addition, following the recent tariff threats from President Trump, Mexico and Canada have both considered retaliatory measures. Nevertheless, early indications appear to reveal a willingness to negotiate a diplomatic resolution.

Observation: The fragility of the trade landscape and what hangs in the balance is already impacting market sentiment and causing businesses to act, rather than take a "hurry up and wait" approach. In the near term, companies should consider prioritizing the calculation of potential impacts on their operations and supply chains, particularly as they assess the risk of disruptions in key regions. Over the long term, the next three years could see heightened retaliatory tariffs on US exports, further emphasizing the need for a proactive and adaptive trade strategy.

Figure 16: North American trade policies are in flux following 2024 developments



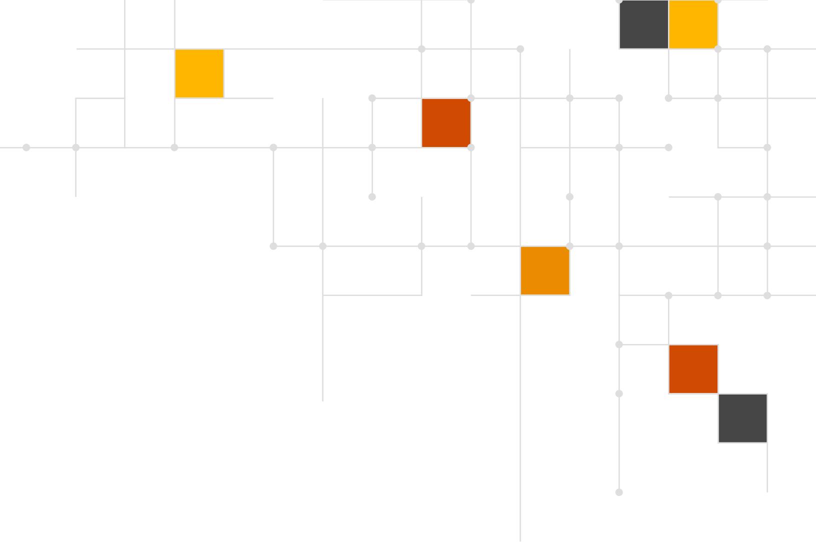
Global four-year horizon

The global trade environment is expected to remain volatile through 2029 and beyond. If the imposition of tariffs on the rest of the world imports (10%–20%) materializes, companies could broaden the scope of supply chain reevaluations over the next four years. The Trump administration's reliance on tariffs as a negotiation tool could provoke retaliatory actions from key partners such as China and Mexico. Additionally, heightened geopolitical tensions may result in new tariffs targeting imports from other countries.

To address these challenges, businesses should conduct forward-looking global modeling to evaluate the impact of tariffs on operations, sourcing strategies, and financial planning. This proactive approach will enable companies to adapt to changes and maintain resilience in an uncertain trade landscape.

Observation: Companies should review multiple operating models to ensure they are fit for purpose over a four-year period. Key areas of review should include the impact of tariffs on the following, looking at the current state situation and expected future state post-imposition of the proposed tariffs:

- Customs mitigation strategies and ability to sustain planning incorporated into existing operating models
- US supply chain procurement model
- US tax operating model — special attention to the impact of Mexico and ROW tariffs
- US transfer pricing model for intercompany purchases to help ensure arm's-length pricing can be sustained.



State tax policy outlook

Many state legislatures will face fiscal uncertainty as they convene their 2025 legislative sessions and approve budgets for the upcoming fiscal year and beyond.

Recent state revenue reports show overall personal and corporate income tax revenue declines, as well as negative growth in inflation-adjusted sales tax revenue. Individual income taxes and sales taxes constitute the two largest revenue sources for most states. Exacerbating the impact of revenue challenges are budgetary decisions that have been made since the pandemic to cut taxes or increase spending.

Other fiscal considerations include the extent to which states rely on federal funds, the increasing cost of delivering services, and the potential for cuts by the new administration (beyond the sunsetting of pandemic-related federal aid). For example, federal funds make up about one-third of California's state budget, and about 75% of those federal funds are used by California to support health and human services spending. New York is estimating its budget gap growing to over $7 billion by 2028, attributable in large part to projected growth in Medicaid costs.

State corporate tax policy outlook

Expected federal legislation addressing corporate tax issues will be the overarching concern of corporate tax policy in the states in 2025. While the timing of such federal legislation remains uncertain, many federal corporate tax policy decisions could have significant state tax consequences.

Business tax provisions that could be addressed in federal tax reform legislation in 2025 include restoring Section 174 expensing for R&D investments, the EBITDA-based business interest limitation under Section 163(j), and 100% bonus depreciation under Section 168(k). Further, under current law, key international business tax rates will increase at the end of 2025 unless addressed by Congress, including the rate of tax on GILTI, BEAT, and FDII.

A key decision for Congress in 2025 will be to agree on the amount of tax relief that can be deficit financed and how much should be offset by some mix of revenue raisers and spending cuts. Among the possible business tax offsets noted above is limiting the federal deduction for state and local tax (SALT) expenses of C corporations, which would make the state corporate tax burden as shown in Figure 17 more material for corporations.

Figure 17: The impact of a change in the federal deduction for corporate state and local taxes could vary depending on levels of business taxes in each state

State	2024 Corporate Tax Rate Top Rate
AK	9.4%
AL	6.50%
AR	4.30%
AZ	4.90%
CA	8.84%
CO	4.25%
CT	8.25%
DC	8.25%
DE	8.7%
FL	5.50%
GA	5.39%
HI	6.40%
IA	7.10%
ID	5.7%
IL	9.50%
IN	4.90%
KS	6.50%
KY	5.0%
LA	7.50%
MA	8.0%
MD	8.25
ME	8.93%
MI	6.0%
MN	9.80%
MO	4.0%
MS	5.0%
MO	4.0%
MS	5.0%
MT	7.0%
NC	2.50%
ND	7.81%
NE	5.84%
NH	7.50%
NJ	11.50%
NM	5.90%
NV	N/A
NY	7.25%
OH	N/A
OK	4.0%
OR	7.60%
PA	8.49%
RI	7.0%
SC	5.0%
SD	N/A
TN	5.0%
TX	N/A
UT	4.55%
VA	6.0%
VT	8.50%
WA	N/A
WI	7.90%
WW	6.50%
WY	N/A

- < 4.00%
- 4.00 - 5.99 %
- 6.00 - 7.99%
- 8.00 - 9.99%
- >9.99%

Source: Thomson Reuters Checkpoint Edge.

Cutting the state corporate tax rate will continue to be an area of interest in some states, following the lead of multiple states in recent years. However, stagnant or declining state revenues could put a damper on the continuation of such tax-cutting and could prompt states to make future tax cuts contingent on achieving revenue targets.

Some states are likely to continue examining different approaches to taxing foreign income, including changes to the combined reporting group or expanding income inclusion rules. An example of this tension has been seen in Minnesota over the last two years. Minnesota lawmakers considered worldwide combined reporting but ultimately adopted a partial GILTI inclusion. Further, in both administrative guidance and controversy, states will continue to develop policies for providing appropriate factor representation of included foreign receipts.

State individual and pass-through entity outlook

Alternative forms of individual taxation are likely to be considered by many states, given the fiscal uncertainty and rising budget deficits. In addition to increasing the rates on their traditional personal income taxes, states could consider enacting capital gains taxes or wealth taxes. For example, Washington State's voters rejected a proposed repeal of the recently enacted capital gains tax in November 2024. In December, outgoing Governor Jay Inslee (D) proposed a new wealth tax to help with the state's multi-billion dollar projected deficit. States are also likely to consider "millionaire's taxes," or rate surcharges on high earners, such as in Illinois, where an advisory ballot measure on this issue was approved.

At the same time, reducing or even eliminating individual income taxes continues to be a focus in some states, especially in those with trifecta Republican control of state government. However, economic conditions, the increased cost of government, and the cumulative impact of prior tax cuts will constrain state policymakers as they seek to achieve these goals. Modest rate relief or phased-in rate reductions with revenue triggers appear to be the most achievable goal in these states.

The impending expiration of the federal SALT cap and potential changes to that limitation also will prompt state action, as the SALT cap effectively increases the tax burden on individual taxpayers especially in high-tax states. Legislative responses are likely in states that have pass-through entity tax regimes that are scheduled to sunset at the same time the federal SALT cap is set to sunset, on December 31, 2025.

States also are looking into the taxation of pass-through entities at the state level more broadly. The Multistate Tax Commission has engaged in a multiyear uniformity project, which most recently has been examining approaches to sourcing income in complex partnership structures. Discussions in recent meetings have raised the issue of creating mandatory taxation of pass-through entities at the entity level, citing the proliferation of pass-through entity regimes in response to the federal SALT cap.

State indirect tax outlook

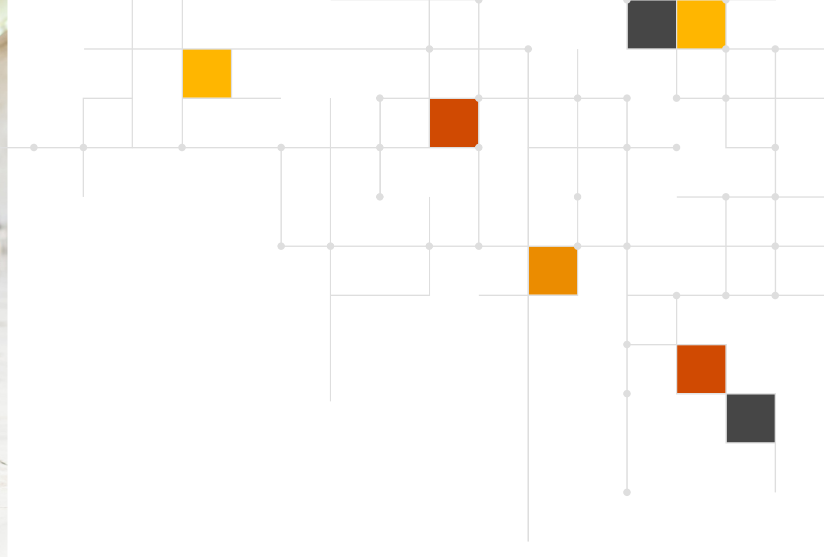
States are likely to continue their consideration of sales tax base expansion measures in 2025. For example, legislation adopted at the close of Louisiana's special session could be a model other states consider. The Louisiana legislation included a franchise tax repeal, income tax cuts, and a corresponding expansion of the sales tax base to include digital products, software-as-a-service, and information services, as well as the repeal of 84 sales and use tax exemptions and exclusions.

Sales tax on digital products and what that encompasses will be front and center in 2025, with legislative proposals likely flowing from ongoing discussions at the Multistate Tax Commission on modernizing the consumption tax base. Virginia, for example, has been holding interim legislative committee hearings regarding the potential application of sales and use tax to digital goods and services, including transactions involving businesses.

Other states are in the process of providing guidance on the taxation of digital goods and services. The Massachusetts Department of Revenue has released a working draft regulation regarding "computer software and related transactions" that updates its existing regulation promulgated over 18 years ago. The Texas Comptroller has proposed changes to its regulation on taxable data processing services, which was last amended 24 years ago. Meanwhile, the California Department of Tax and Fee Administration has been holding workshops to discuss the tax treatment of Technology Transfer Agreements, and a proposal to amend its regulation promulgated in 2002 may follow.

States also appear likely to continue considering proposals to impose digital service taxes based on gross revenue, following Maryland's adoption of a digital advertising tax. The outcome of pending litigation challenging Maryland's tax may influence whether states adopt similar taxes or consider variations intended to avoid legal challenges. States also appear likely to consider "data taxes" based on the use of in-state consumer data, patterned on a multi-year legislative effort to enact such proposals in New York.

Remote seller and marketplace facilitator issues will continue to be considered in the states, including changes to the thresholds for collection requirements and addressing compliance for both marketplace facilitators and sellers. Sourcing continues to be an area of controversy, with multiple challenges being filed in Illinois challenging the state's remote sales law. These challenges allege that the Illinois law discriminates against interstate commerce by imposing destination sourcing on sales by remote sellers and origin sourcing on sales by similarly situated retailers that maintain an Illinois presence.



Appendices

Appendix A: Key policymakers

Congressional leadership in the 119th Congress

House Leadership	
Speaker of the House	Mike Johnson (R-LA)
Majority Leader	Steve Scalise (R-LA)
Majority Whip	Tom Emmer (R-MN)
Republican Conference Chair	Lisa McClain (R-MI)
Republican Conference Vice Chair	Blake Moore (R-UT)
Republican Congressional Campaign Committee Chair	Richard Hudson (R-NC)
Republican Policy Committee Chair	Kevin Hern (R-OK)

Minority Leader	Hakeem Jeffries (D-NY)
Minority Whip	Katherine Clark (D-MA)
Assistant Democratic Leader	Joe Neguse (D-CO)
Democratic Caucus Chair	Pete Aguilar (D-CA)
Democratic Conference Vice Chair	Ted Lieu (D-CA)
Democratic Policy and Communications Committee Chair	Debbie Dingell (D-MI)
Democratic Congressional Campaign Committee Chair	Suzan DelBene (D-WA)

Senate Leadership

President of the Senate	Vice-President JD Vance (R)
President Pro Tempore	Chuck Grassley (R-IA)
Majority Leader	John Thune (R-SD)
Majority Whip	John Barrasso (R-WY)
Republican Conference Chair	Tom Cotton (R-AR)
Republican Policy Committee Chair	Shelley Moore Capito (R-WV)
Republican Conference Vice-Chair	James Lankford (R-OK)
National Republican Senatorial Committee Chair	Tim Scott (R-SC)

Minority Leader and Democratic Conference Chair	Charles Schumer (D-NY)
Minority Whip	Dick Durbin (D-IL)
Democratic Steering and Policy Committee Chair	Amy Klobuchar (D-MN)
Democratic Strategic Communications Committee Chair	Cory Booker (D-NJ)
Democratic Conference Vice-Chairs	Elizabeth Warren (D-MA), Mark Warner (D-VA)
Democratic Outreach Committee Chair	Bernie Sanders (I-VT)
Democratic Conference Secretary	Tammy Baldwin (D-WI)
Democratic Outreach Committee Vice-Chair	Catherine Cortez Masto (D-NV)
Deputy Democratic Conference Secretaries	Brian Schatz (D-HI), Chris Murphy (D-CT)
Democratic Senate Congressional Committee	Kirsten Gillibrand (D-NY)

House and Senate tax-writing committees

House Ways and Means Committee

The Ways and Means Committee currently is composed of 26 Republicans and 19 Democrats.

House Ways and Means Committee Members, 119th Congress

Republicans	Democrats
Chairman Jason Smith (R-MO)	Richard Neal (D-MA), Ranking Minority Member
Vern Buchanan (R-FL)	Lloyd Doggett (D-TX)
Adrian Smith (R-NE)	Mike Thompson (D-CA)
Mike Kelly (R-PA)	John Larson (D-CT)
David Schweikert (R-AZ)	Danny Davis (D-IL)
Darin LaHood (R-IL)	Linda Sanchez (D-CA)
Jodey Arrington (R-TX)	Terri Sewell (D-AL)
Ron Estes (R-KS)	Suzan DelBene (D-WA)
Lloyd Smucker (R-PA)	Judy Chu (D-CA)
Kevin Hern (R-OK)	Gwen Moore (D-WI)
Carol Miller (R-WV)	Don Beyer (D-VA)
Greg Murphy (R-NC)	Dwight Evans (D-PA)
David Kustoff (R-TN)	Brad Schneider (D-IL)
Brian Fitzpatrick (R-PA)	Jimmy Panetta (D-CA)
Greg Steube (R-FL)	Jimmy Gomez (D-CA)
Claudia Tenney (R-NY)	Steven Horsford (D-NV)
Michelle Fischbach (R-MN)	Stacey Plaskett (D-VI)
Blake Moore (R-UT)	Brendan Boyle (D-PA)
Beth Van Duyne (R-TX)	Tom Suozzi (D-NY)
Randy Feenstra (R-IA)	
Nicole Malliotakis (R-NY)	
Mike Carey (R-OH)	
Aaron Bean (R-FL)	
Max Miller (R-OH)	
Nathaniel Moran (R-TX)	
Rudy Yakym (R-IN)	

Senate Finance Committee

The Finance Committee currently includes 14 Republicans and 13 Democrats.

Senate Finance Committee Members, 119th Congress

Republicans	Democrats
Mike Crapo (R-ID), Chairman	Ron Wyden (D-OR), Ranking Minority Member
Charles Grassley (R-IA)	Maria Cantwell (D-WA)
John Cornyn (R-TX)	Michael Bennet (D-CO)
John Thune (R-SD)	Mark Warner (D-VA)
Tim Scott (R-SC)	Sheldon Whitehouse (D-RI)
Bill Cassidy (R-LA)	Maggie Hassan (D-NH)
James Lankford (R-OK)	Catherine Cortez Masto (D-NV)
Steve Daines (R-MT)	Elizabeth Warren (D-MA)
Todd Young (R-IN)	Bernie Sanders (I-VT)
John Barrasso (R-WY)	Tina Smith (D-MN)
Ron Johnson (R-WI)	Ben Ray Luján (D-NM)
Thom Tillis (R-NC)	Raphael Warnock (D-GA)
Marsha Blackburn (R-TN)	Peter Welch (D-VT)
Roger Marshall (R-KS)	

Key Treasury and other Administration officials

Treasury Secretary, *Nominated*	Scott Bessent
Director, National Economic Council	Kevin Hassett
Director, Office of Management and Budget, *Nominated*	Russell Vought
Chair, Council of Economic Advisers	Stephen Miran
Treasury Assistant Secretary for Tax Policy, *Nominated*	Ken Kies
IRS Commissioner, *Nominated*	Billy Long
IRS Chief Counsel	Marjorie Rollinson*

* Rollinson has announced that she plans to retire before the end of the Biden Administration.

Appendix B: Senators up for re-election in 2026

Democrats	Republicans
Booker, Cory (D-NJ)	Capito, Shelly Moore (R-WV)
Coons, Christopher (D-DE)	**Cassidy, Bill (R-LA)**
Durbin, Richard (D-IL)	Collins, Susan (R-ME)
Hickenlooper, John (D-CO)	**Cornyn, John (R-TX)**
Lujan, Ben Ray (D-NM)	Cotton, Tom (R-AR)
Markey, Edward (D-MA)	**Daines, Steve (R-MT)**
Merkley, Jeff (D-OR)	Ernst, Joni (R-IA)
Ossoff, Jon (D-GA)	Graham, Lindsey (R-SC)
Peters, Gary (D-MI)	Hagerty, Bill (R-TN)
Reed, Jack (D-RI)	Hyde-Smith, Cindy (R-MS)
Shaheen, Jeanne (D-NH)	Lummis, Cynthia (R-WY)
Smith, Tina (D-MN)	**Marshall, Roger (R-KS)**
Warner, Mark (D-VA)	McConnell, Mitch (R-KY)
	Mullin, Markwayne (R-OK)
	Ricketts, Pete (R-NE)
	Risch, James E. (R-ID)
	Rounds, Mike (R-SD)
	Sullivan, Dan (R-AK)
	Tillis, Thom (R-NC)
	Tuberville, Tommy (R-AL)

Senate Finance Committee members shown in **bold**

Appendix C: Legal pathways to presidential trade policy executive actions

	What does it do?	Potential measures under this Act	How is it possible?
Sec. 301 of the Trade Act of 1974	Generally, requires the USTR to take certain authorized actions (subject to Presidential direction) if a foreign country's act, policy, or practice: (1) violates, denies, or is inconsistent with the rights or benefits of the United States under any trade agreement, or (2) unjustifiably burdens or restricts US commerce.	• Tariffs or import restrictions on any goods (even if not involved in the act, policy, or practice) of the foreign country. • Suspend, withdraw, or prevent trade agreement benefits. • Alternatives available.	• USTR investigation initiated • Consultation with the foreign country • Affirmative determination (generally within 12 months) • Congress receives semiannual report
Sec. 232 of the Trade Expansion Act of 1962	Presidential authority to adjust imports if the Department of Commerce determines that articles (or their derivatives) are imported in quantities or under circumstances that threaten or impair national security.	• Any action to adjust imports of those articles so they will not threaten or impair national security. • Includes tariffs, quotas, and other import restrictions (e.g. import bans) on the offending goods.	• Commerce investigation (270 days to report), except for emergencies. • Presidential concurrence and action determined (90 days from report to decide, and 15 additional days to implement).
Sec. 201 of the Trade Act of 1974	Requires the President to act if the US International Trade Commission (ITC) determines increased import quantities are a substantial cause of serious injury (or threat thereof) to a domestic industry producing goods like, or directly competitive with, the imported goods.	• Actions to facilitate a positive adjustment to import competition with greater benefits than cost. • Includes tariffs, quotas, import restrictions (e.g. bans) on the offending good. • Alternatives available.	• ITC investigation (120 days), with report to President (180 days) • Presidential determination, recommendation, and implementation (60 days)

	What does it do?	Potential measures under this Act	How is it possible?
International Emergency Economic Powers Act of 1977	Presidential authority to regulate economic transactions if there is an unusual and extraordinary foreign threat to US national security, foreign policy, or economy, if the President declares a national emergency with respect to such threat.	• Includes regulating, preventing, or prohibiting any importation of any property in which any foreign country or a national thereof has any interest by any person. • Not historically the primary legal basis for imposing tariffs or trade restrictions.	• President usually must consult with Congress before exercising these powers, and report to Congress immediately after exercising, with supplemental reports every 6 months
Sec. 338 of the Trade Act of 1930	Presidential authority to retaliate against foreign countries that: (1) impose any unreasonable charge, exaction, regulation, or limitation on imported US goods, or (2) discriminate against imports of US goods.	• Duties up to 50% • Import bans • Forfeiture, seizure, and distribution of imports in violation of the US measures	• ITC investigation, recommendations to the President • Imposed by the Commissioner of Customs
Sec. 122 of the Trade Act of 1974	Presidential authority to address: (1) large and serious US balance-of-payments deficits, (2) imminent and significant depreciation of the US dollar in foreign exchange markets, or (3) international balance-of-payments disequilibrium	• Import surcharges (duties up to 15%) • Quotas if permitted by trade or monetary agreements, only if imbalance cannot be dealt with effectively by a surcharge • Up to 150 days • Non-discriminatory unless 1+ country has large or persistent balance-of-payments surpluses	• Presidential authority to act unilaterally, but address Congress after initial 150 days • Can be extended past 150 days by Congress

For additional information on these and other statutes granting the president authority to act in trade-related matters, see CRS Report R44707, Presidential Authority over Trade: Imposing Tariffs and Duties (updated December 9, 2016); and CRS Report IF11030, US Tariff Policy: Overview (updated October 3, 2024).

Appendix D: Previous efforts to streamline the federal government

Attempts by previous administrations to streamline the federal government to achieve goals related to deficit reduction, governmental efficiency, and effectiveness have had mixed levels of success.

After failed attempts to cut government spending through the OMB, President Ronald Reagan turned to businessman Peter Grace to chair a commission to find potential efficiencies in the federal government. The Grace Commission's 1984 report recommended changes that it maintained could have saved $424 billion in three years and up to $1.9 trillion per year by 2000.

A 1984 report by the CBO and the General Accounting Office (GAO) reviewed 90% of the Grace Commission's deficit reduction recommendations and found that they would have saved only about $98 billion (approximately 33% of the $298 billion savings projected for the recommendations that were reviewed). Although some of the commission's recommendations were adopted by various government agencies, the CBO-GAO report found that several recommendations were vague, lacked the necessary supporting data, and were likely to be applied inconsistently across agencies.

Vice President Al Gore's National Partnership for Reinventing Government (NPR), established in 1993, was intended to streamline the federal government by reducing spending, cutting internal regulations in half, and downsizing the federal workforce. Backed by President Bill Clinton, Gore's reinventing government initiative made 384 recommendations intended to save $108 billion and significantly change the way the federal government operated, including eliminating over 100 programs and 252,000 federal jobs and consolidating over 800 agencies.

Congress responded to NPR's efforts by passing the Government Performance and Results Act (GPRA) requiring agencies to develop strategic and performance plans, measure performance, and publicly report annual progress. By 1995, agencies reported that they had implemented one-third of NPR's original recommendations, resulting in $58 billion in savings. In the same year, NPR proposed about 200 new recommendations, with targeted savings of nearly $70 billion over five years.

By 1998, the size of the federal civilian workforce had been cut by 351,000 and agencies had completed about two-thirds of NPR's original recommendations (generating about $177 billion in savings over five years) and eliminated about 640,000 pages of internal rules and 16,000 pages of Federal Regulations.

The bipartisan National Commission on Fiscal Responsibility, launched by President Barack Obama in 2010, produced an ambitious package that would have combined trimmed Social Security costs and reduced defense funding with restrained tax breaks and increased federal gas taxes. But only 11 of the 18 members of the commission, known as Simpson-Bowles for its Republican and Democratic chairs, former Senator Alan Simpson (R-WY) and former White House Chief of Staff Erskine Bowles, voted for the package, falling short of the 14 supermajority votes required for approval. Only Senators Mike Crapo (R-ID) and Dick Durbin (D-IL), two members of Simpson-Bowles who voted in favor of the plan, remain in Congress.

Appendix E: Congressional Budget Office estimates of select deficit reduction options

Revenue raising provisions

Individual revenue options	Revenue estimate over 10 years ($ billions)
Increase maximum taxable earnings subject to social security payroll taxes	728 - 1,427
Impose a new payroll tax	1,282 - 2,540
Increase individual income tax rates on ordinary income	570 - 1,185
Impose a surtax on individual's adjusted gross income	1, 051 - 1,440
Increase rates on long-term capital gains and qualified dividends by 2 percentage points	103
Eliminate or modify head-of-household filing status	76 - 209
Limit the deduction for charitable giving	324 - 348
Eliminate or limit itemized deductions	736 - 3,424
Change the taxation of assets transferred at death	197 - 536
Eliminate tax exemption for new qualified private activity bonds	43
Expand the base of the net investment income tax to include income of active participants in S corporations and limited partnerships	420
Tax carried interest as ordinary income	13
Include VA's disability payments in taxable income	235
Further limit annual contributions to retirement plans	187
Eliminate certain tax preferences for education expenses	130
Lower the investment income limit for the earned income tax credit and extend that limit to the refundable portion of the child tax credit	11
Require earned income tax credit and child tax credit claimants to have a social security number that is valid for employment	28
Expand social security coverage to include newly hired state and local government employees	149
Increase federal civilian employees' contributions to the federal employees retirement system	40

Business revenue options	Revenue estimate over 10 years ($ billions)
Reduce tax subsidies for employment-based health insurance	521 - 965
Increase the corporate income tax rate by 1 percentage point	136
Repeal the LIFO, lower of cost or market, and subnormal goods inventory methods	104
Require half of advertising expenses to be amortized over 5 or 10 years	83 - 177
Repeal the low-income housing tax credit	69

Other revenue options	Revenue estimate over 10 years ($ billions)
Impose a tax on financial transactions	297
Increase taxes on alcoholic beverages	88 - 102
Increase excise taxes on tobacco products	51
Increase excise taxes on motor fuels and index for inflation	212
Impose a 5% value-added tax	2,180 - 3,380
Impose a tax on emissions of greenhouse gasses	645 - 919

Spending reduction provisions

Mandatory spending options	Savings over 10 years ($ billions)
Establish caps on federal spending for Medicaid	459 - 893
Limit state taxes on health care providers	48 - 612
Reduce federal Medicaid matching rates	69 - 561
Increase premiums paid for Medicare Part B	510
Reduce Medicare Advantage benchmarks	489
Change the cost-sharing rules for Medicare and restrict Medigap insurance	20 - 129
Reduce Medicare's coverage of bad debt	17 - 54
Consolidate and reduce Medicare payments for graduate medical training at teaching colleges	94 - 103
Modify payments to Medicare Advantage plans for health risk	124 - 1,049
Reduce payments for hospital outpatient departments	6 - 157
Reduce payments for drugs by 340B hospitals	15 - 74

Reduce Social Security benefits for high earners	48 - 197
Establish a uniform Social Security benefit	283 - 607
Raise the full retirement age for Social Security	95
Require Social Security Disability Insurance applicants to have worked more in recent years	60
Introduce means-testing for eligibility for VA's disability compensation	384
Use an alternative measure of inflation to index Social Security and other mandatory programs	278

Discretionary spending options	**Revenue estimate over 10 years ($ billions)**
Reduce the Department of Defense's annual budget by approximately 10% by (1) reducing the number of active military personnel, (2) reducing ground and air combat units, (3) de-emphasizing the use of US combat forces, and/or (4) relying on allies to provide more of their own defense.	959
Reduce funding for international affairs programs	187
Reduce selected nondefense discretionary spending by reducing grants to state and local governments for transportation (i.e., highway and transit grants) and education programs (i.e., funding for the education of children from low-income households and of children with disabilities).	339

Source: CBO, Options for Reducing the Deficit: 2025 to 2034 (December 2024)

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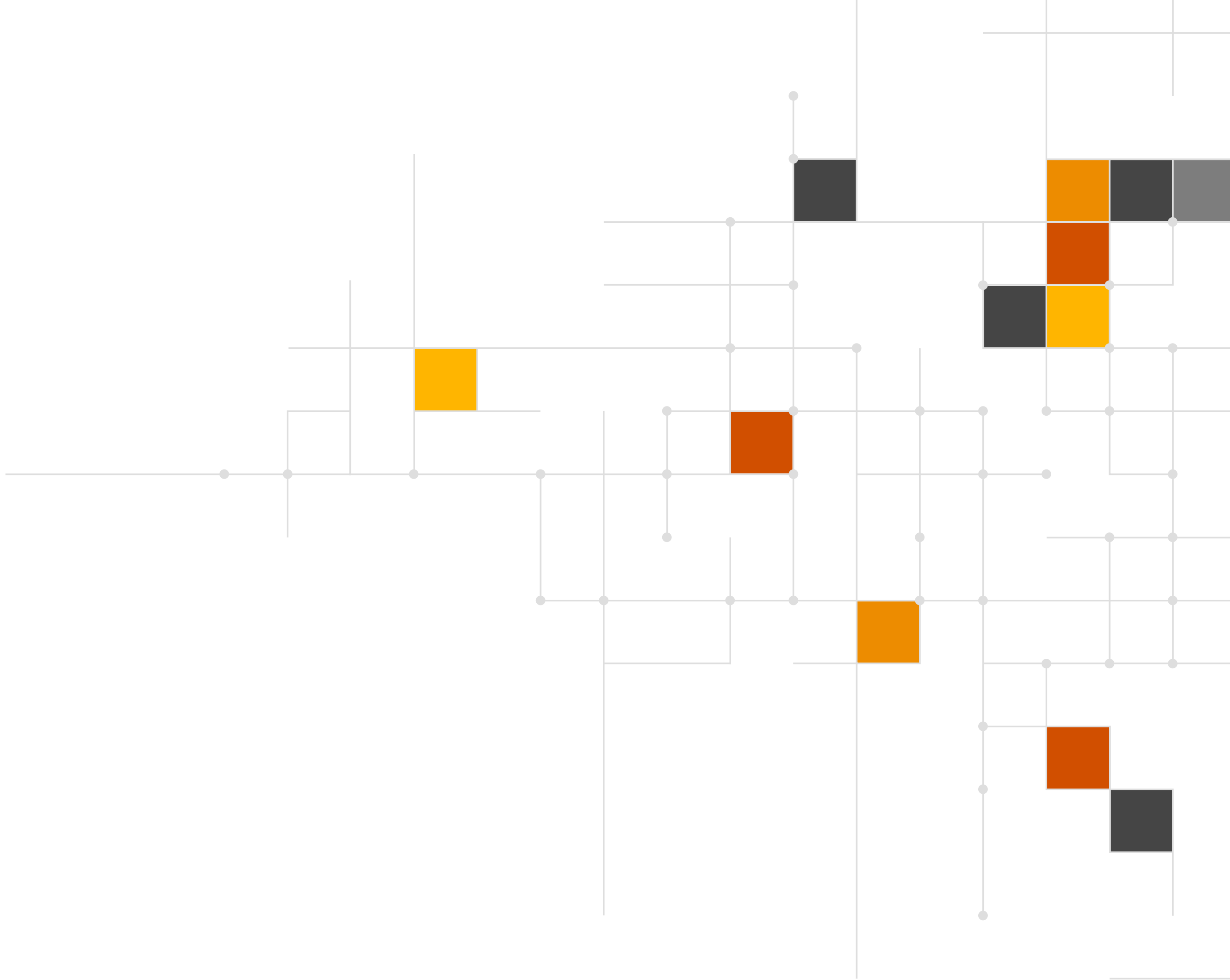

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