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Reading the tea leaves: Potential tax legislation in the new Congress

The 2022 mid-term election has shifted the scales in Washington, D.C., with the Democrats no longer controlling both houses of Congress. While it remains to be seen if — and when — any tax-related legislation can muster the requisite bipartisan support, a review of certain provisions in existing laws may provide an indication of the many areas ripe for action in the next two years.

Retirement catch-ups at risk

The SECURE 2.0 Act, enacted at the tail end of 2022, reportedly includes a technical drafting error that jeopardizes the abilities of taxpayers to make catch-up contributions to their pre-tax or Roth retirement accounts. According to the American Association of Pension Professionals and Actuaries, under the existing statutory language, no participants will be able to make such contributions beginning in 2024.

The American Retirement Association has brought the issue to the attention of the U.S. Department of Treasury and the Joint Committee on Taxation (JCT), a nonpartisan congressional committee that assists with federal tax legislation. While the JCT has apparently acknowledged that the language does appear to be a drafting error, a timely correction is far from guaranteed.

Indeed, such "technical corrections" legislation once passed Congress routinely. However, it has proven more challenging in the political climate of the last decade or so. For example, it took three years for Congress to pass minor corrections to the first SECURE Act. And a glitch in the Tax Cuts and Jobs Act of 2017 (TCJA) affecting eligibility for bonus depreciation wasn't corrected until the CARES Act became law in 2020.

Expiring tax provisions

Tax-related legislation often includes so-called "sunset" dates — the dates tax provisions will expire, absent congressional action. For example, the Consolidated Appropriations Act, enacted in 2021, boosted the allowable deduction for business meals from 50% to 100% for 2021 and 2022. In 2023, the deduction limit returned to 50%.

A JCT report released in January 2023 highlights numerous significant provisions that are scheduled to expire in coming years without congressional action to extend them. For example, several tax credits related to renewable and alternative energy will expire at the end of 2024.

But 2026 is the year when some of the most wide-reaching and particularly valuable provisions – many of them created or modified by the TCJA – are set to disappear. They include:

- Lower individual tax rates,
- Enhancements to the Child Tax Credit (CTC),
- Health insurance premium tax credit enhancements,

Expiring tax provisions (continued)

- The New Markets Tax Credit,
- The employer credit for paid family and medical leave,
- The Work Opportunity Tax Credit,
- The increase in the exemption amount and phaseout threshold for the alternative minimum tax,
- The increase in the standard deduction,
- The suspension of the miscellaneous itemized deduction,
- The suspension of the limit on itemized deductions,
- The income exclusion for employer payments of student loans,
- The suspension of the deduction for personal exemptions,
- The limit on the deduction for qualified residence interest,
- The suspension of the deduction for home equity interest,
- The limit on the deduction for state and local taxes,
- The qualified business income deduction,
- The deduction percentages for foreign-derived intangible income and global intangible low-taxed income,
- Empowerment zone tax incentives, and
- The increase in the federal gift and estate tax exemption.

At the end of 2026, bonus depreciation also is slated for elimination. In fact, the allowable deduction already has dropped from 100% to 80% of the cost of qualified assets in 2023. The limit will drop by 20% each year until vanishing in 2027.

Expired tax provisions

Several notable provisions expired or changed at the end of 2021, despite chatter in Washington about the possibility of extensions. For example, as of 2022, taxpayers can no longer deduct Section 174 research and experimentation expenses, including software development costs, in the year incurred. Rather, they must amortize these expenses over five years (or 15 years if incurred outside of the United States). In addition, the calculation of adjusted taxable income for purposes of the limit on the business interest deduction has changed, potentially reducing the allowable deduction for some taxpayers.

Individuals also saw the end of several tax provisions at the end of 2021, including the:

- CTC expansions created by the American Rescue Plan for some taxpayers,
- Expanded child and dependent care credit,
- Increased income exclusion for employer-provided dependent care assistance,
- Treatment of mortgage insurance premiums as deductible mortgage interest,
- Charitable contribution deduction for non-itemizers, and
- Increased percentage limits for charitable contributions of cash.

It's possible that some of these could be included in any "extender" legislation Congress might consider this year or next.

The FairTax Act

Unlikely to see much progress, however, is the proposed FairTax Act. Although it has the support of a group of U.S. House Republicans, GOP House Speaker Kevin McCarthy has stated that he doesn't support the legislation.

The FairTax Act (continued)

The bill would eliminate most federal taxes — including individual and corporate income, capital gains, payroll and estate taxes — as well as the IRS. It would replace the taxes with a 23% federal sales tax on goods and services, which couldn't be offset by deductions or tax credits. The plan has been around for two decades and has yet to garner a floor vote, an indicator of its odds this time around — especially with Democrats in control of the U.S. Senate.

Ear to the ground

Congress may not feel a sense of urgency to address tax provisions that aren't set to expire for three years, but the catch-up contribution error would have substantial repercussions for many taxpayers in less than a year. We'll let you know if lawmakers take action on this or any other important tax matters that could affect you. Contact us for more information.
