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TAX ALERT – MAY 2025

The U.S. House of Representatives Passes the "One Big Beautiful Bill Act"

Introduction

On May 22, 2025, the U.S. House of Representatives passed the "One Big Beautiful Bill Act" (H.R. 1), (the "**Act**"), which is comprised of over one thousand pages. The Act must be approved by the U.S. Senate before the President can sign it into law.

The Act makes the 2017 Tax Cuts and Jobs Act tax cuts permanent, preventing their scheduled expiration after 2025, introduces additional tax cuts, eliminates approximately $1.5 trillion of government spending and raises the debt ceiling by $4 trillion, preventing the U.S. from the risk of default.

In addition to provisions affecting individual taxation - such as certain exemptions on tips and overtime pay, an increase in the estate and gift tax exemption to $15 million for individuals ($30 million for married couples), and an increase in the maximum deduction for State and local taxes from $10,000 to $40,000 for taxpayers earning under $500,000 - there are several provisions affecting business taxation and U.S.-inbound investment by foreign persons.

We describe some of the Act's most notable provisions below.

Business Tax Provisions

Research or Experimental ("R&E") Costs. Taxpayers may deduct domestic R&E expenses or elect to capitalize and amortize them. Taxpayers must continue to capitalize and amortize foreign R&E expenditures over 15 years. The effective date is for taxable years beginning on or after January 1, 2025.

Interest Expense Limitation. The Act modifies the interest expense limitation under Internal Revenue Code ("**IRC**") Section 163(j) from 30% of earnings before interest and taxes (or "EBIT") to 30% of earnings before interest, taxes, depreciation, and amortization (or "EBITDA"). The effective date is for taxable years beginning on or after January 1, 2025.

Reduction of Inflation Reduction Act's ("IRA") Renewable Energy Tax Credits. The Act reduces or phases out the IRA's renewable energy tax credits.

Fixed Assets Depreciation. The Act reintroduces the 100% first-year "bonus depreciation" through 2029 (2030 for certain property), increases the IRC Section 179 deduction cap to $2.5 million, and provides for a 100% depreciation allowance for certain commercial qualified production property.

Qualified Business Income Deduction. The Act increases from 20% to 23% the IRC Section 199A deduction for qualified business income (pass-through businesses like partnerships, S-corporations, and sole proprietorships).

Qualified Opportunity Zones ("QOZ"). The Act renews the QOZ program for taxable years 2027 through 2033 to encourage investments in rural areas of the country and provides benefits that include temporary deferral of capital gains taxes, tax basis step-up and exclusions from taxable income.

International Tax Rules for Inbound Investment

Tax Rate Increase on U.S. Source Income of Certain Foreign Persons. The Act introduces important new measures that significantly impact inbound investment in the U.S., including an annual tax rate increase of 5 percentage points over the statutory rates (or any rate of tax applicable in lieu of such statutory rate), until such increase has reached a maximum of 20 percentage points over the statutory rates (the "**Additional Tax**"). The Additional Tax would be applicable on U.S. source income of certain residents of countries with "unfair" tax regimes that impose extraterritorial or discriminatory taxes and implicitly override existing U.S. income tax treaties ("**Discriminatory Countries**").

Extraterritorial, discriminatory taxes include a digital services tax ("**DST**"), and the OECD's "Global Anti-Base Erosion Model Rules (Pillar Two)" ("**Pillar Two**").

- ***DST***. In February of 2025, the U.S. President directed a review and possible renewal of investigations into countries that have implemented DSTs specifically targeting France, the U.K., Italy, Spain, Austria, Turkey and Canada. A 2021 report on Italy's DST issued by the Office of the United States Trade representative had identified 43 companies that would meet Italy's DST revenue thresholds. Of those, 27 companies (or over 62%) were U.S. companies, and only 3 companies (less than 7%) were Italian companies. The report concluded that the disparity between these results indicates that the revenue thresholds have a discriminatory effect.

- ***Pillar Two***. Most EU Member States have enacted Pillar Two in their domestic legislation pursuant to the EU Pillar Two Directive (Council Directive (EU) 2022/2523). However, these Pillar Two top-up tax systems, which provide for a global minimum tax of 15% for large multinationals, may conflict with a pre-existing bilateral tax treaty in place between an EU country, which has adopted Pillar Two, and a non-EU country, such as the U.S., that has not adopted Pillar Two. On January 20, 2025, the President of the U.S. signed an Executive Order stating that Pillar Two has no force or effect in the U.S.

Under proposed new IRC Section 899, the Additional Tax applies to foreign corporations, with respect to U.S. effectively connected income ("**ECI**"), currently subject to a 21% tax rate, including gains from the disposition of U.S. real property, U.S. fixed or determinable annual or periodic ("**FDAP**") income, such as dividends, interest, royalties, and rents, currently subject to a 30% tax rate, and the branch profits tax, currently subject to a 30% tax rate. The Additional Tax also applies to nonresident aliens, but only with respect to FDAP income and gains from the disposition of U.S. real property, and to foreign private foundations, with respect to the federal excise tax imposed on certain income.

To the extent U.S.-source income is subject to a lower tax rate pursuant to a U.S. income tax treaty, the Additional Tax applies to such lower treaty rate. For example, dividends that would otherwise be subject to a reduced 5% tax rate pursuant to a U.S. income tax treaty with a discriminatory foreign country would be subject to a 10% tax rate (5% Treaty rate, plus 5% Additional Tax) for the first year. The Additional Tax would increase by an additional 5 percentage points for each one-year period after the Applicable Date (as defined below). However, the rate increases are limited such that the overall rate cannot exceed the relevant statutory rate (determined without regard to any rate applicable in lieu of such statutory rate) by more than 20 percentage points. This means, for example, that dividends eligible for a 5% treaty rate can eventually be subject to a 50% rate over the years (the statutory 30% rate, plus 20%).

Effective Date. The Additional Tax applies to taxable years beginning after the later of (i) 90 days after the date of enactment of the Act, (ii) 180 days after the date of enactment of the unfair foreign tax that causes such country to be treated as a discriminatory, and (iii) the first date that the unfair foreign tax begins to apply; and before the last date on which the discriminatory foreign country imposes an unfair foreign tax (the **"Applicable Date"**). For example, assuming the Act is enacted prior to October 1, 2025, the Additional Tax would apply to tax years beginning on or after January 1, 2026, for foreign persons that are residents of a discriminatory country. However, the tax rate increases on withholding taxes apply with respect to a person for each calendar year beginning during the period that such person is a resident of a country that is listed as a discriminatory foreign country by the Secretary.

Base Erosion Anti-Abuse Tax ("BEAT"). BEAT is an additional tax imposed on certain corporations that are members of a multinational group with respect to payments to foreign affiliates. The BEAT generally applies to corporate taxpayers that are members of a group with average gross receipts in excess of $500 million and is determined, in part, by the extent to which a taxpayer has made base erosion payments ("**BEP**") to foreign related parties. The BEAT generally does not apply when base erosion payments are less than 3% percent of total deductions. The BEAT was originally scheduled to increase from a 10% tax to 12.5% beginning in 2025. The Act increases the BEAT tax rate to just 10.1%, except as provided below.

The Act would expand the application of the BEAT to a foreign-owned non-public corporation, if more than 50% of the stock of such corporation, by vote or value, is held, directly or indirectly, by residents of a Discriminatory Country. Under these circumstances, the BEAT would apply regardless of the average annual gross receipts test and the base erosion percentage test and, in addition, the applicable BEAT tax rate would be 12.5%. Furthermore, payments that would otherwise be excluded from the definition of BEP because they are capitalized (e.g., qualifying interest or royalties) would be considered BEP. Similarly, for these corporations, payments for services eligible for the use of the "services cost method" under IRC Section 482 would be a BEP and a BEP subject to U.S. withholding tax would not be reduced for amounts on which tax is withheld,

Other International Tax Rules

The Act would slightly modify the current rates for Global Intangible Low-Taxed Income ("**GILTI**") and Foreign-Derived Intangible Income ("**FDII**"), discussed below.

GILTI. The current deduction for GILTI (including the IRC Section 78 gross-up) of 50% would be reduced to 49.2%, resulting in a 10.668% rate.

FDII. FDII is currently taxed at a rate of 13.125% by means of a 37.5% deduction under IRC Section 250. The Act would change the deduction to 36.5%, resulting in a tax rate of 13.335%.