CLEARY GOTTLIEB

ALERT MEMORANDUM

U.S. Congress Passes 'One Big Beautiful Bill': Tax Aspects

July 3, 2025

On July 3, 2025, Congress passed and sent to the President for his signature the "One Big Beautiful Bill Act" (the "Act"), which among other things makes permanent many provisions of 2017's Tax Cuts and Jobs Act (the "TCJA") that otherwise would have expired this year, and introduces several important changes to the tax system, in particular concerning R&E expenses and international tax issues.

Notably, the final law *omitted several provisions* discussed at various stages of the legislative process, including: changes to the taxation of carried interest, the so-called "revenge tax" penalizing countries for implementing certain types of taxes, a provision to make ineffective the "SALT workaround" or pass-through entity taxes, and a proposed litigation financing tax.

What's New(ish) for Businesses: The Act makes permanent certain business provisions that expired or were set to expire under the TCJA (with some modifications).

— *Permanent Expensing of R&E*: Taxpayers may deduct domestic research and experimentation expenses beginning in 2025. (Since 2022, these expenses needed to be capitalized and amortized over 5 years.) Foreign research and experimentation expenses will continue to be amortizable over 15 years.

— *Permanent Bonus Depreciation*: Taxpayers may immediately deduct 100% of the cost of certain depreciable tangible property.

— *Permanent Change to Net Interest Expense Deduction*: The limitation on the deduction of net interest expense is calculated at 30% of EBITDA rather than the more restrictive EBIT. (Since 2022, the limitation has been calculated using EBIT.)

If you have any questions concerning this memorandum, please reach out to your regular firm contact or the following authors

NEW YORK

Kylie N. Barza
+1 212 225 2164
kbarza@cgsh.com

Matthew Brigham
+1 212 225 2102
mbrigham@cgsh.com

Swift Edgar
+1 212 225 2736
sedgar@cgsh.com

Jason R. Factor
+1 212 225 2694
jfactor@cgsh.com

Meyer H. Fedida
+1 212 225 2747
mfedida@cgsh.com

William L. McRae
+1 212 225 2188
wmcrae@cgsh.com

Susanna Parker
+1 212 225 2913
sparker@cgsh.com

Jonathan Gifford
+1 212 225 2279
jgifford@cgsh.com

SAN FRANCISCO

Maureen Linch
+1 415 796 4420
mlinch@cgsh.com

What's New:

— *Changes to International Taxation:*

- *Increased Taxation of Non-U.S. Operations—Net CFC Tested Income (the new name for what was formerly "Global Intangible Low-Taxed Income"* or GILTI): In addition to the GILTI regime's new name, notable changes include:
  - Increasing the effective tax rate to 14% from 13.125% (after taking into account allowable foreign tax credits, in each case);
  - Eliminating the deduction for a 10% deemed return on "qualified business asset investments" (*i.e.*, depreciable property known as "QBAI"); and
  - Modifying the allocation of expenses in calculating foreign tax credits and increasing the amount of such foreign taxes that may be credited (from 80% to 90%).
- *Reduction to the Tax Benefits for Exports—Foreign-Derived Deduction Eligible Income or FDDEI (the new name for what was formerly "Foreign-Derived Intangible Income" or FDII)*: In addition to renaming the FDII deduction, notable changes include:
  - Increasing the effective tax rate on such income to 14% from 13.125%; and
  - Excluding from the calculation of FDDEI (and thus from the benefit of the reduced tax rate):
    - Income and gain from the sale or exchange (or deemed sale or deemed exchange) of intangible property or property that is subject to depreciation, amortization, or depletion; and
    - Interest expense and research and experimentation expenses.
- *Fixing "Downward Attribution"*: The Act restores the "downward attribution" rule in section 958(b)(4), which was removed by the TCJA in order to address a policy concern but had the effect of radically increasing the number of entities treated as controlled foreign corporations, and instead now addresses that policy concern through a more targeted provision.
- *Base Erosion and Anti-Abuse Tax or BEAT*: The BEAT tax rate is permanently set at 10.5% (and 11.5% for members of affiliated groups that include a bank or registered securities dealer).

— *Miscellaneous Changes*:

- *New Charitable Deduction Floors*:
  - *Corporations*: Corporations may take deductions for charitable contributions only to the extent they exceed 1% of, and do not exceed 10% of, the taxable income of the corporation.
  - *Individuals*: Individuals who itemize deductions may take charitable deductions only to the extent the charitable deductions exceed 0.5% of adjusted gross income. The Act also creates a new deduction for charitable contributions for non-itemizing individuals.
- *University Endowment Tax*: The Act expands the excise tax on net investment income of university endowments into a graduated tax based on the ratio of endowment assets to students (the "student adjusted endowment"), which range from 1.4% (for institutions with a student adjusted endowment of at least $500,000 and not more than $750,000) to 8% (for institutions with a student adjusted endowment of more than $2,000,000). These rates are significantly lower than the rates proposed in the initial House-passed bill, which included a top rate of 21%.
- *Disguised Sales:* A contribution to a partnership, together with a related distribution by the partnership, if properly viewed as a sale, is now more clearly treated as a disguised sale

in the absence of regulations. (This had been a long-standing source of debate among tax practitioners.)

- *Qualified Small Business Stock*: The Act replaces the 5-year holding period requirement for the exclusion for gain on the sale of qualified small business stock with a tiered exclusion based on the holding period of stock acquired after the date of enactment. After a 3-year holding period, the exclusion is 50%; after 4 years, 75%; and after 5 years, 100%.
- *Opportunity Zones*: The Opportunity Zone regime is permanent, with modifications and special rules for rural areas.

— *Changes to Individual Taxation*:

- *SALT Cap*: The Act raises the cap on the deduction for state and local taxes from the current law $10,000 to $40,000 in 2025 for individuals and married couples filing jointly earning less than $500,000. The cap and the income limitation increase by 1% each year through 2029 before the cap drops back down to $10,000 in 2030.
- *Repeal of Miscellaneous Itemized Deductions*: Miscellaneous itemized deductions are permanently repealed.
- *Limitation on Itemized Deductions*: For individuals in the highest tax bracket (37%), the value of itemized deductions is reduced to $0.35 on the dollar to the extent of an individual's income taxed at that highest marginal rate.
- *Limitation on Excess Business Losses*: The limitation on excess business losses of noncorporate taxpayers is permanent.
- *Campaign Promises*: The Act includes limited deductions for tips and overtime pay, as well as a deduction for senior citizens (designed to have the effect of reducing tax on social security payments).
- *Estate Tax*: The Act increases the estate and gift tax exemption to $15 million ($30 million for married filers), makes the exemption permanent, and indexes it for inflation.

— *Clean Energy Tax Credits*: The bill makes a number of modifications, phase-outs, and terminations to various tax credits for renewable energy, energy efficiency, and manufacturing. We will address those changes in detail in a future memorandum.

Much ado About Nothing—What Stays the Same: Below are some provisions that were either proposed in prior iterations of the Act or proclaimed as part of President Trump's agenda, and which were ultimately left out of the Act.

— *Carried Interest*: Holders of carried interests continue generally to enjoy capital gain treatment, assuming a more than 3-year holding period.

— *Pass-Through Entity Taxes*: Partners and other investors in pass-through entities continue to be able to reduce their taxable income by certain state and local taxes paid at the entity level, a partial work-around to the TCJA's cap on the state and local tax deduction.

— *Section 899 (a/k/a the "Revenge Tax")*: Both the initial House-passed bill and the initial Senate version of the bill added a provision that would have significantly increased the rate of withholding taxes and certain other taxes on governments and residents of countries that enact an "unfair foreign tax"—for example, undertaxed profits rules—as well as on U.S. corporations owned by such residents. That tax would have affected many of the United States's main trading partners (*e.g.*, Australia, Canada, EU members, Japan, UK). While under consideration, this "revenge tax" was heavily criticized as having the potential to stifle foreign investment in the United States. The final version of the Act does not include the revenge tax.

- Secretary Treasury Bessent announced an agreement among the G7 countries that the revenge tax would be removed from the Act in exchange for an exemption for U.S. corporations from certain non-U.S. taxes.

- The revenge tax would have targeted countries that have enacted digital services taxes or diverted profits taxes, but the Trump administration has indicated it intends to use tariffs to pressure countries to repeal such taxes.

— *Third-Party Litigation Funding Excise Tax*: The Act left out a new excise tax (proposed by the Senate) on certain proceeds received by third-party investors who fund litigation in exchange for a contingent financial interest therein.

— *Increases to Private Foundation Tax*: The tax on net investment income of private foundations remains at 1.39%. The initial House-passed bill would have increased the rate to up to 10% (depending on the size of the foundation's assets).

— *Sports Team M&A*: The Act omits a provision that was in the initial House-passed bill which would have limited the amortization deductions for the intangible property associated with the acquisition of sports franchises to 50%.

— *Qualified Business Income*: The Act retains the deduction for qualified business income (*i.e.*, certain pass-through income) at 20%, albeit with some modifications.

…

CLEARY GOTTLIEB