

Senate set to clear pared-down ‘CHIPS’ bill with tax break for US semiconductor makers

After Democratic Sen. Joe Manchin of West Virginia recently blocked his party’s efforts to pass expansive “Build Back Better” legislation before Congress adjourns for its August recess, the Senate this week shifted gears and appears poised in the coming days to clear bipartisan legislation designed to boost domestic semiconductor manufacturing and encourage US research activities. However, while the measure includes an investment tax credit intended to promote domestic production of semiconductors, it appears unlikely that lawmakers will add a provision that would retroactively permit expensing for research expenditures under section 174.

CHIPS Act of 2022

Senate consideration of the CHIPS Act of 2022 (H.R. 4346: text; section-by-section summary) came relatively swiftly after Sen. Manchin pointedly withdrew—at least for now—his support for Democrats’ broader effort to, among other things, raise taxes on corporations and high-income individuals, address climate change, and reduce the budget deficit as part of their Build Back Better initiative. (See related coverage in this issue for details on Manchin’s decision and the more limited Build Back Better legislation that Democrats now appear poised to move instead.)

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Importantly, the iteration of CHIPS legislation currently moving through Congress is actually the offspring of a much more expansive “China competition” package that Democrats and Republicans had been attempting to hash out in a 107-member, House-Senate conference committee. However, the two chambers were struggling to resolve key differences between their respective bills, which led to the late-stage effort to pass a narrower bill focused primarily on boosting domestic semiconductor production.

“We worked very hard to get a bill out of the Senate. We got overwhelming votes for it, and then when we got to the House, we hit a brick wall,” said Senate Foreign Relations Committee Chairman Bob Menendez, D-N.J., whose committee’s entire contribution to the Senate’s original China competition package was struck for the narrower bill.

“It’s a shame,” Menendez continued. “Because it’s [now] a chips bill, not a China bill.”

25 percent investment tax credit *plus* funding for domestic chip makers: The new package, which the nonpartisan Congressional Budget Office (CBO) estimates will cost roughly \$80 billion over 10 years, leans heavily on direct funding aimed at building, expanding, and modernizing domestic semiconductor facilities, along with boosting funding for research and development programs administered by the Department of Commerce.

[URL: https://www.cbo.gov/system/files?file=2022-07/hr4346_chip.pdf](https://www.cbo.gov/system/files?file=2022-07/hr4346_chip.pdf)

On the tax side, the bill would create a 25 percent investment tax credit (under new tax code section 48D) for “qualified property”—generally, tangible and depreciable or amortizable property—that is constructed or acquired new by the taxpayer and is integral to the operation of a facility for which the primary purpose is the manufacture of semiconductors or equipment used in semiconductor manufacturing. The provision would also allow taxpayers, including partnerships and S corporations, to receive the credit under a direct-pay option (similar to the direct-pay provisions for delivering certain clean energy tax incentives in the House-approved version of the Build Back Better Act).

The credit, which carries a 10-year cost of roughly \$25 billion according to the CBO, generally would be available for property placed in service after December 31, 2022, and for which construction begins before January 1, 2027.

Extension of research expensing still on the sidelines: Though the policy maintains broad bipartisan support, the CHIPS legislation being considered in the Senate does not include language aimed at reversing a change within tax code section 174—originally enacted as part of the Tax Cuts and Jobs Act of 2017 (P.L. 115-97)—that, as of January 1 of this year, requires certain research expenditures to be amortized over a number of years rather than deducted currently.

For his part, Senate Finance Committee member Todd Young, R-Ind., blamed Democrats for insisting that any section 174 relief be provided alongside an extension of enhancements to the Child Tax Credit that were enacted last year as part of Democrats’ American Rescue Plan and also expired at the start of 2022.

“For whatever reason, it is in their mind attached, and our nation’s innovation is frankly being held hostage to their insistence on a particular type of child tax [credit],” Young said.

If any section 174 change remains left out of the CHIPS bill—as seems likely—advocates will likely have to wait until the post-election lame duck session later this year, when that and a number of other revenue policies (related to retirement tax policy and expired and expiring provisions collectively known as “tax extenders”) will also likely be in play as part of a potential year-end tax-and-appropriations package.

CHIPS enactment appears likely

Senate Minority Leader Mitch McConnell, R-Ky, had indicated in no uncertain terms earlier this month that Republicans would withhold support for any CHIPS-related legislation so long as Democrats were pursuing a larger-scale Build Back Better bill under the budget reconciliation process; however, after Sen. Manchin said he could not back Democrats’ Build Back Better effort, the legislative gears on CHIPS began moving once again.

In fact, 16 GOP senators joined nearly all Democrats July 19 in a 64-34 procedural vote on a so-called “shell” bill designed to kick off debate on semiconductor-related legislation. Then, on July 20—after filing a substitute amendment to that bill in the form of the 1,054-page CHIPS Act of 2022—Senate Majority Leader Charles Schumer, D-N.Y., filed cloture on the underlying legislative package. That new legislative text is expected to come up for another procedural vote as early as July 25, with final approval expected as soon as July 27.

Although votes are still being rounded up, and notwithstanding potential amendments that may be incorporated into the legislation, reports currently suggest that the House—aided by what is expected to be continuing strong bipartisan Senate support—is likely to take up and pass the CHIPS bill and send it to President Biden’s desk before lawmakers in that chamber adjourn for their summer recess, which is scheduled to begin on July 29.

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