With lame duck session set to begin, balance of power in 118th Congress remains unclear

With Election Day now behind them, House and Senate lawmakers are about to return to Washington for their lame duck legislative session to close out the current Congress and prepare for the start of the next one. But with a number of House and Senate races still undecided following this week's congressional midterms, questions still linger regarding the balance of power in the two chambers for the upcoming 118th Congress, which convenes in January, and just how those questions are resolved may shape what lawmakers can get done as the current Congress enters its final days.

According to results reported by C-SPAN (based on data from the Associated Press) as of press time, neither Democrats nor Republicans have secured the 218 seats required for a majority in the House of Representatives. Democrats have clinched 192 seats, while Republicans have won 211. Votes are still being counted in the remaining 32 races.

Across the Rotunda, Democrats will control at least 48 seats in the Senate and Republicans will hold at least 49. Results of still-undecided Senate races in Arizona and Nevada likely will be finalized in the coming days as vote counts are completed. The undecided race in Georgia will be resolved in a runoff election on December 6 between Democratic incumbent Democratic Sen. Raphael Warnock and Republican challenger Herschel Walker. (None of the three candidates in Georgia's Senate contest received at least 50 percent of the vote in this week's general election and state law requires a runoff between the top two vote-getters in those circumstances.)

The Alaska Senate race also remains undecided, but the top two candidates in that contest—incumbent Sen. Lisa Murkowski and challenger Kelly Tshibaka—are both Republicans, so that seat is expected to remain in GOP hands regardless of who emerges as the victor.

Deloitte Tax LLP will release more detailed discussions of the election results and their potential implications for tax policy as we gain more clarity on how control of Congress will shake out next year.

Lame duck overview

Under the current schedule for the upcoming work period, both chambers will be in session the week of November 14, adjourn the week of November 21 for the Thanksgiving recess, then reconvene the week of November 28 and remain in session through at least mid-December.

Dominating that first week back will be a flurry of administrative activity, such as new member orientation and training, office lotteries, and box packing and farewell parties for departing lawmakers. Democrats and Republicans in both chambers also are expected to hold elections during the lame duck to choose their respective leaders for the next Congress. House Republicans have scheduled their leadership elections for November 16. Leadership elections for House Democrats are set for November 30. Party leadership elections in the Senate have not yet been scheduled.

Topping the lame duck legislative agenda will be funding federal government operations. Lawmakers have not yet agreed on a spending measure for fiscal year 2023, which began on October 1, and are currently keeping the government's doors open through a short-term continuing resolution (approved in September) that funds federal departments and agencies at fiscal year 2022 levels through December 16. Once the lame duck session begins, Congress will be under pressure to clinch a funding deal for the remainder of this fiscal year or, alternatively, to adopt another continuing resolution that likely would extend into 2023. Any funding measure that clears the House and Senate also may include supplemental emergency spending for additional aid to Ukraine and disaster relief related to Hurricane Ian and Hurricane Fiona.

A host of other issues also will be clamoring for lawmakers' attention before the end of the year—for example, several new and proposed tax code changes (more on those below), Electoral Count Act reforms, and marriage equality codification—but action on any of these items likely will depend on the extent to which the two parties are in a mood to compromise as they come back from the campaign trail. In addition, if the midterm results ultimately determine that Democrats will lose control of the Senate next year, Majority Leader Charles Schumer, D-N.Y., may prioritize using scarce Senate floor time to confirm judges and other administration nominees in the remaining days of the 117th Congress.

Year-end tax wish list

Although there is no comprehensive tax bill currently moving through either chamber, lawmakers in both parties see the lame duck session as an opportunity to address assorted tax priorities, such as reversing or deferring certain base-broadening provisions enacted in the Tax Cuts and Jobs Act (TCJA, P.L. 115-97), passing certain family-focused tax incentives that were left out of the recently enacted Inflation Reduction Act (P.L. 117-169), renewing expired and expiring tax "extenders" provisions, and advancing another round of retirement security legislation.

Any tax items that can win consensus among lawmakers during the lame duck session may be packaged into an omnibus bill with a long- or short-term government funding measure. (Certain items that have bipartisan support may resurface on the legislative agenda in the next Congress if they are not addressed in the lame duck.)

Tax treatment of research expenses: There has been strong bipartisan support in both chambers for repealing or deferring a change within tax code section 174—originally enacted as part of the TCJA—that, as of January 1 of this year, requires certain research expenditures to be amortized over a number of years rather than deducted immediately.

A provision in the Build Back Better Act that cleared the House last November would have allowed expensing for an additional four years before again returning to required amortization. That measure subsequently stalled in the Senate, however, and the proposed section 174 provision was not incorporated into the Inflation Reduction Act (the successor to Build Back Better that was signed into law in August). According to an estimate by the Joint Committee on Taxation (JCT) staff, the provision in the House-passed legislation would have

increased the deficit by about $4 billion over the 10-year budget window.
URL: https://www.jct.gov/publications/2021/jcx-46-21/

Business interest expense limitation, bonus depreciation: In addition to the section 174 modification, lawmakers also might seek to reverse two other changes enacted in the TCJA.

The first change, which took effect at the beginning of this year, generally requires companies to calculate their adjusted taxable income based on earnings before interest and taxes (EBIT) as opposed to earnings before interest, taxes, depreciation, depletion, and amortization (EBITDA) for purposes of applying the limitation on deductions of net business interest expense.

The second change generally calls for the bonus depreciation rate for most qualified property to be reduced from 100 percent to 80 percent beginning in 2023, with additional reductions of 20 percentage points in each successive year until the bonus rate reaches 20 percent in 2026 and falls to zero thereafter.

Enhanced child tax credit: Many congressional Democrats are expected to continue their push for a long-term extension of enhancements to the child tax credit that were enacted in 2021 as part of the American Rescue Plan and expired at the end of last year. House Democrats included a one-year extension of the enhanced credit (through 2022) in their Build Back Better legislation; however, Senate Democratic leaders left that provision out of the Inflation Reduction Act to help ensure the measure's passage in that chamber. As part of their lame duck negotiations, Democrats hoping to provide tax relief for low- and moderate-income taxpayers this year may seek to use a more generous child tax credit as a bargaining chip in exchange for their support of certain business-focused tax provisions sought by Republicans.

The JCT staff has estimated that the one-year extension of the enhanced credit in the House-approved Build Back Better legislation would have reduced federal receipts by nearly $185 billion over the 10-year budget window, and that a permanent extension would reduce federal receipts by more than $1.2 trillion (under conventional scoring methods) and nearly $1.4 trillion (under "dynamic" scoring methods that take into account certain macroeconomic effects of the provision) over the same period. Lawmakers could seek to reach agreement on a compromise proposal that expands the credit but at a lower cost to the fisc, although at this point neither side has signaled an interest in moving to the middle on this issue.
URL: https://www.jct.gov/publications/2021/jcx-46-21/
URL: https://gop-waysandmeans.house.gov/wp-content/uploads/2022/11/117-1113.pdf

SALT deduction cap: Congressional Democrats representing jurisdictions with high local income and property taxes may well resume their longstanding efforts to eliminate or relax the current-law $10,000 cap on the deduction for state and local taxes (SALT), which was enacted in the TCJA and is scheduled to expire after 2025.

The House-passed version of the Build Back Better Act called for temporarily increasing the cap on the deduction to $80,000. Members of what has become known as the "SALT Caucus" had vowed to block the Inflation Reduction Act if it did not include a similar provision, although they ultimately backed down from that position and SALT relief was left out of the enacted measure. Congressional Republicans, for their part, generally appear intent on making the cap permanent.

Traditional extenders: Congress also faces decisions about a variety of expired and expiring temporary tax "extenders" provisions benefiting businesses and individuals. While the Inflation Reduction Act addressed a host of temporary provisions related to renewable energy and energy efficiency, other extenders have been expired since the end of 2021 or are set to lapse at the end of this year. (A complete list of temporary provisions—which does not reflect changes enacted in the Inflation Reduction Act—is available from the JCT staff.)
URL: https://www.jct.gov/publications/2022/jcx-1-22/

Additional miscellaneous tax items: A handful of other items that have constituencies arguing for their enactment as part of a potential year-end tax package also could come into play. These provisions include relief from more stringent 1099 reporting requirements for so-called third-party payment processors that were enacted in the American Rescue Plan and took effect this year, relief from last-in, first-out (LIFO) inventory recapture rules for car dealers impacted by recent supply chain issues, and various tax "technical corrections" to both the Tax Cuts and Jobs Act and the Inflation Reduction Act.

Retirement security: There is bipartisan, bicameral support for enacting another round of retirement security protections that would build on 2019's SECURE Act, particularly in light of the fact that two prominent boosters of retirement legislation—House Ways and Means Committee ranking member Kevin Brady, R-Texas, and Senate Finance Committee member Rob Portman, R-Ohio—did not seek re-election this year and will leave Capitol Hill when the 117th Congress expires.

The House overwhelmingly approved a bipartisan "SECURE 2.0" bill (H.R. 2954) this past March. (For prior coverage, see *Tax News & Views*, Vol. 23, No. 13, Apr. 1, 2022.) The Senate Finance Committee unanimously cleared its version of a SECURE 2.0 measure in June. (For prior coverage, see *Tax News & Views*, Vol. 23, No. 22, June 24, 2022.) Finance Committee Chairman Ron Wyden, D-Ore., and ranking member Mike Crapo, R-Idaho, formally introduced that proposal (S. 4808) in the Senate on September 8.
URL: https://www.congress.gov/bill/117th-congress/house-bill/2954/text/eh
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2022/TNV/220401_1.html
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2022/TNV/220624_1.html
URL: https://www.congress.gov/bill/117th-congress/senate-bill/4808/text

Both bills include provisions that, broadly speaking, are aimed at making it easier for businesses to offer tax-qualified retirement savings plans to their employees and for individuals to participate in retirement plans and grow their tax-preferred savings. The JCT estimates that both bills would generate relatively modest increases in federal receipts over the 10-year budget window, primarily by offsetting forgone revenue with provisions that would make certain retirement accounts and retirement account contributions subject to after-tax "Roth" treatment.

A new IRS commissioner?: Another potential item on the lame duck agenda is consideration of Danny Werfel to replace IRS Commissioner Charles Rettig, whose statutory five-year term expires on November 12. The

White House announced on November 10 that the president intends to nominate Werfel to that post. (See separate coverage in this issue for additional details.)

Once he is formally nominated, Werfel will have to be vetted by the Senate Finance Committee and confirmed by the full Senate. Wrapping up the process by the end of this year likely would be an ambitious undertaking and it is highly possible that action could spill over into the new Congress. However, as already noted, if Republicans are poised to take control of the chamber in January, current Majority Leader Charles Schumer may seek to prioritize this and other nominations while he is still in a position to set the agenda and confirm individuals for these positions without Republican votes.

The Treasury Department announced October 28 that Doug O'Donnell, who is currently the IRS Deputy commissioner for services and enforcement, will serve as acting IRS commissioner once Rettig steps down and will continue in that role until a new commissioner is confirmed.

Debt ceiling: There has been some talk of using the lame duck session to enact another extension of the federal debt ceiling. The most recent such extension (S.J. Res. 33), which was signed into law late last year, increased the federal statutory borrowing cap to roughly $31 trillion, an amount that according to the latest estimates is likely sufficient to ensure the nation can continue to pay its bills into at least the second half of 2023. A more precise projection of when the government would risk defaulting on its debt absent further congressional action on the debt ceiling is not currently available.
URL: https://www.congress.gov/bill/117th-congress/senate-joint-resolution/33/text

As a practical matter, however, time is a valuable commodity in a lame duck session and lawmakers may be reluctant to devote a great deal of it to the debt ceiling—especially if the Senate ultimately flips to GOP control and Sen. Schumer opts to focus on advancing as many nominees as possible while he is still majority leader.

If Congress does not address the debt ceiling during the lame duck session, some congressional Republicans have indicated that they may consider using that issue as leverage next year and seek to gain concessions from the White House on certain fiscal issues, such as cutting spending to address inflation, in exchange for their support of a debt ceiling increase. They could also seek to link it to action on nonfiscal issues, such as an expansion of energy exploration and production on federal lands. Any attempt by Democrats to raise the debt ceiling this year likely could be viewed, at least in part, as an effort to prevent Republicans from leveraging the issue to try to force other policy changes in 2023.

Action on tax priorities not guaranteed

Despite the wide range of tax priorities that lawmakers might address in the wake of the midterms, it's important to keep in mind that the breadth of an eventual lame duck bill—and whether that package will include any tax provisions—is not yet clear. The resolution of questions around control of the House and Senate in the next Congress will play a significant role in setting expectations for what can happen in a year-end legislative session since each party's appetite for striking a deal may increase—or diminish—based on how they perceive their relative power both before and after the 118th Congress officially convenes next January.

Moreover, to the extent a deal is possible, the sheer volume of issues in play could make for complex and difficult negotiations, and lawmakers would need to be careful to avoid producing a bill so big that it collapses under its own weight.

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