

# TCJA 2.0: Tax Cuts, Tariffs and Revenue Raisers

February 3, 2025

Tax law change is in the air. Republican congressional leaders are focused on extending the provisions of the 2017 Tax Cuts and Jobs Act (“TCJA”) that are set to expire at the end of 2025, including individual income tax rate cuts and the enhanced child tax credit, and implementing President Trump’s tax campaign promises. On Saturday, President Trump jumped in with an executive order imposing a hefty 25% tariff on imports from Mexico and Canada and a 10% tariff that applies to China.

## **TAX LAW CHANGE WILL COME THROUGH BUDGET RECONCILIATION PROCESS**

Given the narrow Republican majority in the Senate, tax legislation will need to advance using the legislative process called “reconciliation,” the same process used to enact both the TCJA and the Inflation Reduction Act of 2022 (“IRA”). This involves setting a congressional budget that establishes a budget shortfall target. Any costs in excess of the target need to be offset with revenue raising provisions of the new legislation.

## **WHAT TYPES OF TAX CUTS AND INCREASES ARE BEING CONSIDERED?**

The House Ways and Means Committee recently kicked off the reconciliation process with a hearing on “The Need to Make Permanent the Trump Tax Cuts for Working Families.” And a 50-page menu of potential budget reconciliation proposals (“proposals”) was circulated on January 17, 2025. These proposals include reductions in income tax rates, expansions of tax credits and tariff proposals. The list is a first cut. Some proposals contradict one another, and others are mutually exclusive. However, the proposals are a starting place for evaluating which tax cuts may move forward and which areas are being targeted for the tax revenue needed to pay for extending the TCJA and implementing the new tax cuts.

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## POTENTIAL CHANGES TO SCORING RULES COULD IMPACT THE REVENUE RAISERS THAT ARE REQUIRED

The hefty cost of extending the TCJA provisions and implementing President Trump's campaign proposals will require a significant amount of revenue raisers to comply with budget reconciliation requirements. The amount of revenue raisers needed will depend on the size of the deficit agreed to in the budget process and how proposals are scored. Tariff proposals are on the list, suggesting that tariff revenues could count as revenue raisers.

Senator Crapo, who chairs the Senate Finance Committee, is a leading proponent of using a so-called "current policy" baseline for scoring purposes. Unlike the usual "current law" baseline, a "current policy" baseline generally ignores the future cost expiring tax provisions and assumes that current tax rates and tax provisions representing the current policy are the appropriate baseline. This approach effectively allows an end run with respect to prior tax cuts that were paid for on the basis that they would expire. The change would dramatically reduce the scoring cost of extending the TCJA, and in turn, the number of revenue raisers that would be required to meet reconciliation requirements. Changing the scoring rules doesn't change real economic costs, but proponents of the change take the view that increased tax revenue attributable to growth will ease this pressure.

It bears watching whether Congressional scoring will switch to a current policy baseline, or if alternatively, Republican leaders simply use the purported rightness of a "current policy" perspective to provide political cover for agreeing to a higher budget deficit.

## WHAT'S ON THE LIST?

### Border-Related Revenue Raisers

- An **across-the-board 10 percent tariff on all imports** is estimated to raise \$1.9 trillion. Tariffs are used as a significant cost-recovery mechanism.
- A **border adjustment tax**, which is a destination-based tax on imported goods into the United States, with a parallel exemption system for exports, is estimated to raise \$1.2 trillion.

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**Debevoise Comments:**

- The 25% Canada and Mexico tariffs exceed the 10% baseline in the list but would not constitute a durable revenue raiser if they're used as leverage to trade for policy concessions.
- A border adjustment tax would represent a major reworking of the US international tax system. US businesses would not be allowed to deduct the cost of imported goods and services but would be exempt from tax on income from exports of goods and services. A border adjustment tax was considered and rejected at the time of TCJA.

**Green Energy Tax Credit Repeal**

- The budget menu includes several provisions to roll back various green energy tax credits to raise \$1.2 trillion over 10 years.

**Debevoise Comment:**

- Despite the attractiveness of the high revenue score, a full repeal of such credits seems unlikely given the widespread popularity of many of the credits. Targeted repeals are more likely.

**SALT Cap Relief or Pain**

- The \$10,000 cap on the state and local taxes ("SALT") deduction for individuals has been a major source of consternation for Republican members from high-tax states, who want an increase in the cap.
- The proposals include several alternative proposals to address the SALT deduction, from complete elimination of the deduction (\$1 trillion revenue) to increasing the cap from \$10,000 to \$15,000 for individuals and \$30,000 for married couples (\$500 billion cost).
- A proposal to eliminate a business SALT deduction also is included, raising \$310 billion. The fact that the list includes changes that would increase the effective tax rates on businesses shows the effect of changing political winds.

**Other Big Ticket (but Radical) Revenue Raisers on the List**

- The elimination of the **home mortgage interest deduction** would raise \$1 trillion. There are other related proposals to instead lower the home mortgage interest deduction cap to \$500,000 from the current \$750,000.

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- An elimination of the **exclusion of interest on state and local government bonds**, ending the favorable treatment of municipal bonds, is estimated to raise \$250 billion.

**Debevoise Comment:**

- Changes in these long-standing and popular tax provisions would be highly controversial within the Republican party, and given the narrow majorities, would be difficult to pass into final legislation.

**Other Notable Proposals**

- A reduction in the **corporate tax rate to either 20% or 15%** is estimated to cost \$73 billion and \$522 billion, respectively. As a result of the large price tag, the full reduction to 15% seems likely to face obstacles.
- Reestablish **immediate expensing of R&D costs**, which is estimated to cost \$169 billion.
- The proposals estimate a \$222 billion cost associated with **repealing the corporate alternative minimum tax** (“CAMT”), which was enacted as part of the IRA. Even though Republicans have decried the CAMT and expressed a desire to repeal it, it remains to be seen if the conviction holds given a repeal would dig a bigger deficit hole to fill.
- Eliminations of **taxes on tips, overtime and income for Americans abroad** reflect President Trump’s campaign promises and, if passed, are estimated to cost approximately \$956 billion.
- The elimination of **estate taxes** is included and is estimated to cost \$370 billion. The threshold for an estate to be taxed is set to drop from ~\$14 million to ~\$7 million next year.
- IRS enforcement funding cuts of \$20 billion, which are estimated to cost \$46 billion.

**WHAT DIDN'T MAKE THE INITIAL LIST?**

At this early stage of the legislative process, it is not possible to “rule in” or “rule out” specific proposals. However, given the many items included in the menu, it may be noteworthy to highlight the following few items that were not included:

- any increase to the 1% stock buyback excise tax on publicly traded companies;

- restoration of the broader interest deductibility limitation to include depreciation and amortization (i.e., the “DA” in “EBITDA”) to increase the amount of allowable interest deductions; and
- restoration of 100% expensing of certain capital expenditures.

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We will continue monitoring the progress of proposals throughout the year and assessing their potential impact on our clients. Please do not hesitate to contact us with any questions.



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