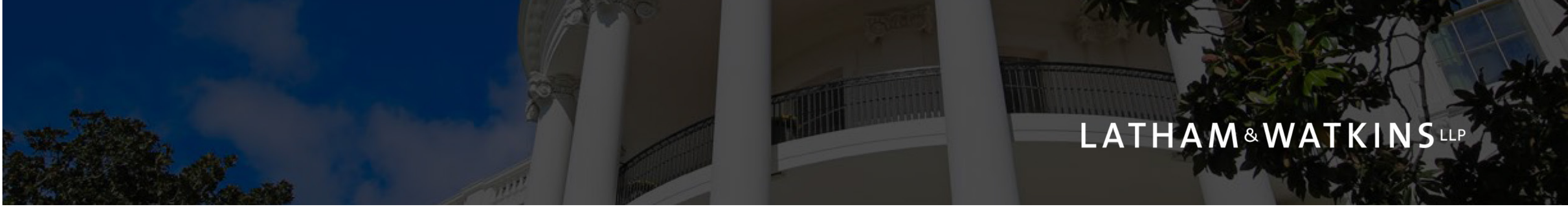
LATHAM & WATKINS LLP

One Big Beautiful Bill: Key Business and Investment Impacts

The Act makes permanent many expiring TCJA provisions and changes key features of US tax law applicable to businesses and investments

August 2025



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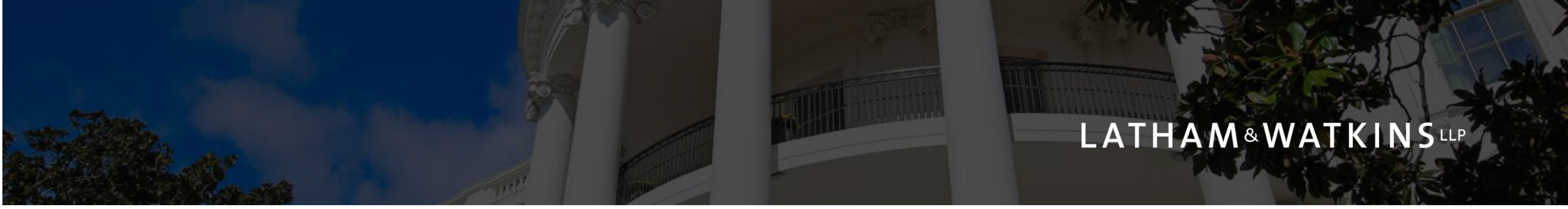


Overview

On July 4, 2025, President Trump signed into law H.R. 1, known as the One Big Beautiful Bill Act (the Act).[1] The Act changes key features of US tax law.

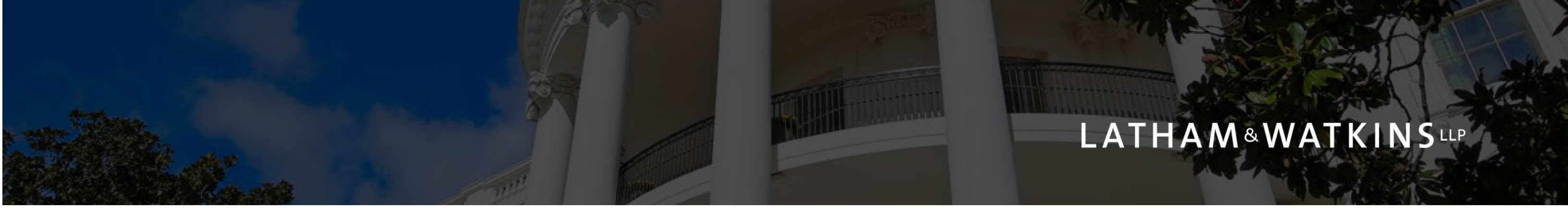
Notably, the Act:

- Makes permanent the Section 199A[2] pass-through entity deduction, 100% first-year bonus depreciation, expensing of research and experimental costs, reduced limitation on business interest deductions, lower individual tax rates, and certain other provisions that were set to expire under the 2017 Tax Cuts and Jobs Act (TCJA)
- Implements significant changes to the international tax regime
- Renews and enhances incentives for Qualified Opportunity Zones and qualified small business stock (QSBS)

This report analyzes and illustrates aspects of the Act relating to a range of taxpayer issues.

[1] https://www.congress.gov/bill/119th-congress/house-bill/1/text.

[2] All references to "Section" are to sections of the Internal Revenue Code of 1986, as amended (the Code), unless otherwise indicated.



I. Pass-Through Entity Provisions

A. Reduction of Tax Rate on Qualified Business Income Made Permanent

The Act makes permanent the Section 199A deduction for qualified business income (QBI), which was created by the TCJA and was set to expire at the end of 2025. The Act generally leaves the 20% deduction unchanged but increases the amount of income a taxpayer must have to be fully subject to certain limitations on the Section 199A deduction, and creates a minimum deduction of $400 for taxpayers whose aggregate QBI from all qualified trades or businesses in which the taxpayer materially participates is at least $1,000 for the taxable year. The amendments become effective January 1, 2026.

Observations:

Section 199A was adopted by the TCJA to effectuate one of the key premises of the TCJA — that corporate and noncorporate business income should be treated more similarly. Under the TCJA, the top corporate rate was permanently lowered from 35% to 21%. Although the top individual tax rate was only lowered from 39.6% to 37% (and only until the end of 2025), Section 199A afforded individuals (as well as trusts and estates) an additional deduction of up to 20% of QBI from a partnership, S corporation, or sole proprietorship until the end of 2025. Thus, for individuals who paid tax at the TCJA top marginal rate of 37%, the deduction generally resulted in a top 29.6% effective tax rate on QBI (without taking into account the possible application of the 3.8% Medicare surtax), which brought the effective noncorporate business income tax rate closer to the corporate rate while keeping the rate for individual investment income and compensation income high. By making permanent the Section 199A deduction and the reduced individual top marginal rate (see Part VIII.A), the Act maintains the status quo for taxpayers considering whether to conduct business in corporate or noncorporate form.

B. Disguised Sale Rules Made Self-Implementing

Prior to the Act, under Section 707(a)(2), contributions of property to a partnership and related distributions could be treated as disguised sales of property or disguised sales of partnership interests to the extent provided in regulations prescribed by the Treasury Secretary. The Act makes this provision self-implementing by eliminating the requirement for regulations and provides the provision is effective and only subject to exceptions provided by the Treasury Secretary. This change applies to transactions after July 4, 2025.

Observations:

There was previously uncertainty regarding whether Section 707(a)(2) could apply to a transaction in the absence of applicable Treasury regulations. This uncertainty was primarily an issue with respect to disguised sales of partnership interests under Section 707(a)(2)(B) because no applicable Treasury regulations have been issued. While the Act's changes to Section 707(a)(2) clarify that applicable Treasury regulations are not required for a transaction to be treated as a disguised sale under Section 707(a)(2)(B), we expect continued uncertainty in determining whether a contribution of property to a partnership by one partner and a related distribution to another partner should be properly characterized as a sale or exchange of a partnership interest — including, in certain cases, contributions and distributions relating to the admission of investors to investment funds. It may be clear that such a disguised sale of a partnership interest has occurred when one partner contributes cash or other property to a partnership, and the partnership — on the same day and pursuant to a plan — uses that cash or other property to redeem another partner. However, it will be more difficult to apply this rule when the contribution and redemption are more attenuated in time and/or purpose.

II. Full Expensing of Certain Capital Investments

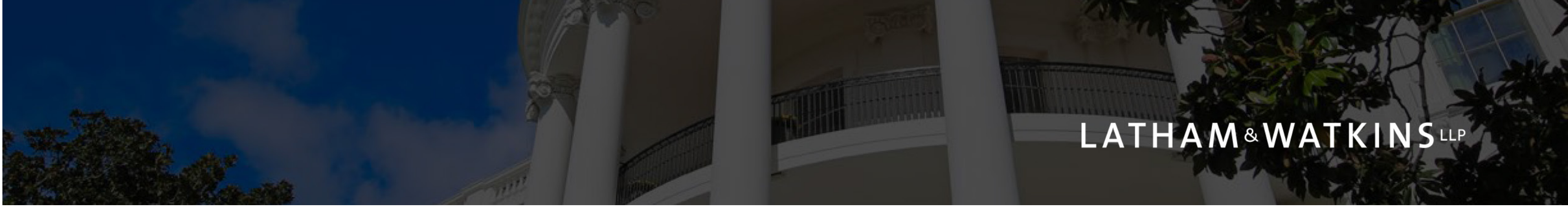
The Act reinstates and makes permanent the 100% first-year bonus depreciation deduction for qualified property (generally, tangible property with a recovery period of 20 years or less and certain computer software) acquired after January 19, 2025. Under the TCJA, 100% first-year bonus depreciation applied through 2022 and then the applicable percentage phased down over the following five-year period until first-year bonus depreciation ultimately expired in 2027. For property acquired before January 19, 2025, prior law is still in effect.

The Act also creates a new 100% first-year bonus depreciation deduction for certain manufacturing, production, or refining facilities located in the United States or its possessions. Such property may include real property with a recovery period of more than 20 years that would not otherwise qualify for first-year bonus depreciation. The facility must begin construction between January 19, 2025, and January 1, 2029, and must generally be placed into service before January 1, 2031.

In addition, the Act introduces a transitional election for reduced first-year depreciation for assets acquired prior to January 20, 2025, and placed in service during the first tax year ending after January 19, 2025. If the election is made, the taxpayer will benefit from 40% first-year depreciation, or 60% for aircraft and certain property with a recovery basis of at least 10 years and other transportation property.

Observations:

- The Act significantly reduces the cost of domestic manufacturing, production, or refining facilities that would otherwise have not qualified for accelerated first-year depreciation.
- Asset acquisitions may result in increased up-front tax benefits as significant amounts of the purchase price may produce immediate deductions.
- The election for reduced first-year depreciation could be beneficial for corporations that would generate



net operating losses (NOLs) with 100% first-year bonus depreciation, but would be in a taxable position if the corporation fully elected out of accelerated first-year depreciation. NOL carryforwards to subsequent taxable years may be less desirable than future depreciation deductions because NOL carryforwards are generally only available to offset 80% of a corporation's taxable income in any particular tax year, whereas depreciation deductions are not subject to this limitation.

III. Restoration of Expensing Research and Experimental Costs

The Act restores the immediate deduction of domestic research and experimental (R&E) expenditures incurred after December 31, 2024. Pursuant to the TCJA, beginning in 2022, domestic R&E expenditures were generally required to be amortized ratably over a five-year period. Taxpayers may elect out of immediately deducting domestic R&E expenditures and instead elect to amortize domestic R&E expenditures ratably over no less than 60 months, beginning with the month in which the taxpayer first realizes benefits from such expenditures. The Act does not change the treatment of foreign R&E expenditures, which are still generally subject to a 15-year amortization period. Certain small businesses may elect to amend their past returns to apply the new Section 174A rules to domestic R&E expenditures incurred after December 31, 2021. The Act allows other taxpayers an election to deduct any remaining unamortized amounts from R&E expenditures in 2022-2024 either in the first taxable year beginning after December 31, 2024, or ratably over the first two taxable years beginning after December 31, 2024.

Observations:

The ability to choose whether to immediately expense domestic R&E expenditures or elect to amortize them over time will allow taxpayers more flexibility to match their deductions with expected taxable income, allowing them to defer deductions in situations in which they would otherwise generate NOL carryforwards.

IV. Business Interest Deduction Limitation Changes and Coordination With Capitalization Rules

Under Section 163(j), corporations and pass-through entities generally must defer deductions of business interest in excess of 30% of "adjusted taxable income" (with certain adjustments). The Act makes the following permanent changes to the definition of adjusted taxable income:

- Any deduction for depreciation, amortization, or depletion is added back. This addback was previously only applicable to taxable years beginning before January 1, 2022, but the Act extends this addback to taxable years beginning after December 31, 2024.

- Certain income attributable to being a US shareholder (generally, a US person holding 10% or more of the equity interests, by vote or by value) in a foreign corporation under Sections 951(a), 951A(a), and 78 is subtracted. This subtraction is applicable to taxable years beginning after December 31, 2025.

The Act also extends the limitation under Section 163(j) to interest that is required to be capitalized under the Code (subject to certain exceptions for straddles and certain self-produced property). To implement this requirement, the Act creates a new ordering rule that requires taxpayers to first allocate permitted interest under Section 163(j) to interest that is required to be capitalized, and then to interest that is deductible.

Observations:

- The change in the definition of adjusted taxable income is generally favorable for taxpayers that incurred depreciation, depletion, and amortization deductions, creating a potentially greater amount of interest that may be deducted, which could reduce the after-tax cost of debt financing. On the other hand, the exclusion of certain income attributable to being a US shareholder in controlled foreign corporations (CFCs) from adjusted taxable income reduces available interest deductions and potentially increases the tax cost of debt financing by a US shareholder.
- As discussed in Part II, under the Act, taxpayers may recognize increased depreciation or amortization deductions attributable to certain capital expenditures. As a result of the Act's changes to Section 163(j), these additional depreciation or amortization deductions should not impact a taxpayer's business interest expense limitation.
- Prior to the Act, taxpayers could work around the Section 163(j) limitation by capitalizing interest and recovering it through another type of tax deduction (e.g., cost of goods sold, depreciation, amortization, or losses), allowing the taxpayer to deduct interest that would otherwise be subject to the Section 163(j) limitation. The Act's limitation on capitalized interest and new ordering rule would generally prevent such workarounds.

V. International Tax Reform

The Act includes several important changes to the post-TCJA international tax regime as outlined below. Importantly, and as a relief to many multinational groups and non-US investors in debt and equity of US issuers, the Act does not include "revenge taxes" that had been included as a new Section 899 in prior versions of the Act and would have imposed significant retaliatory taxes on persons with connections to certain countries that had enacted one or more "unfair foreign taxes."

A. Restriction on Downward Attribution Partially Restored

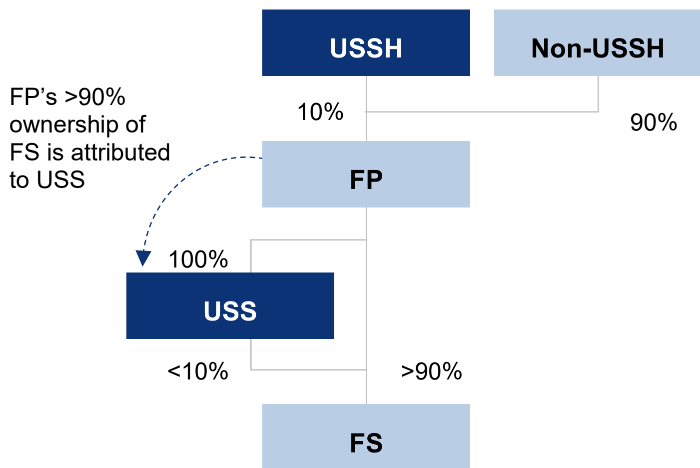
US shareholders of CFCs are subject to a multitude of special rules under the Code. For this purpose, a US shareholder with respect to a foreign corporation is a US person who is treated as owning 10% or more of the equity interests (by vote or value) of a foreign corporation, and a CFC is a foreign corporation with more than 50% of its equity interests (by vote or value) owned by 10% US shareholders. Prior to the enactment of the TCJA, attribution of ownership of stock to other entities owned by the stockholder (commonly referred to as "downward attribution" of stock ownership) from a foreign person to a US person was disregarded for purposes of identifying US shareholders and CFCs. The TCJA repealed this limitation, thus greatly expanding the number of entities treated as CFCs even if there was no direct or indirect 10% US shareholder. For example, the foreign affiliates of a widely held foreign-parented public group would be considered CFCs solely by reason of a US affiliate in the group to which ownership would be attributed post-TCJA. Such expansion has been generally viewed as reaching beyond intragroup "de-control" structures that were the initial target of the repeal.

The Act generally reverses the TCJA's repeal of the limitation on downward attribution of stock ownership from a foreign person to a US person, but with an important exception. The Act creates a new Section 951B, which generally applies the CFC inclusion rules to "foreign controlled United States shareholders" (FC-US shareholders) of "foreign controlled foreign corporations" (FC-CFCs). An FC-US shareholder is generally the same as a US shareholder, except that downward attribution is taken into account and the applicable ownership threshold is 50% instead of 10%. An FC-CFC is the same as a CFC except it looks to ownership by FC-US shareholders instead of US shareholders and takes into account downward attribution. The general restoration provision combined with the addition of new Section 951B is consistent with the stated policy goals of TCJA of targeting certain de-control structures, for example group planning following the acquisition of a US multinational group by a foreign parent corporation.

Observations:

- These changes are generally expected to significantly reduce the number of foreign corporations that are treated as CFCs, providing welcome relief.
- Credit agreements, bond indentures, and other similar financing documents with US borrowers often exclude CFCs from guarantee requirements or place limitations on the pledge of CFC equity. Both borrowers and lenders should review the applicable agreements to assess any impact on the guarantor and/or collateral requirements.
- An effect of the new Section 951B is to cause US subsidiaries in a foreign-parented group that have a direct or indirect interest in a foreign subsidiary of that group to continue to be subject to the CFC inclusion rules, while relieving unrelated US shareholders from the CFC inclusion rules. Foreign-parented groups will have to evaluate the impact of Section 951B on their structures.

Figure 1: Example of New Downward Attribution Rules



Description
USSH is a US person (individual or corporation), and USS is a US corporation. Non-USSH is not a US person. Each of FP and FS is a foreign corporation.

Regular CFC Rules
Absent downward attribution, neither USS nor USSH would be subject to CFC income inclusions with respect to FS because FS is not treated as a CFC in the absence of downward attribution (i.e., less than 50% of its equity interests are treated as owned by US shareholders).

New Section 951B
USS (but not USSH) is subject to CFC income inclusions with respect to FS. USS is an FC-US Shareholder of FS because it is treated as owning more than 50% of its equity interests as a result of downward attribution. FS is an FC-CFC because more than 50% of its equity interests are treated as being owned by USS, an FC-US Shareholder.

As a result, new Section 951B subjects USS to CFC income inclusions with respect to FS. New Section 951B has no effect on USSH because USSH is not treated as owning more than 50% of FS regardless of downward attribution.

B. Changes to Pro Rata Share Rules for CFCs

A US shareholder is generally required to include in its income its pro rata share of Subpart F and global intangible low-taxed income (GILTI), which is modified and renamed as net CFC tested income (NCTI) under the Act as discussed in Part V.C. Under pre-Act law, a US shareholder only has a pro rata share inclusion if it is treated as owning stock of the CFC on the last day of the year on which the CFC was treated as a CFC, regardless of which other shareholders owned the CFC at other times in such year.

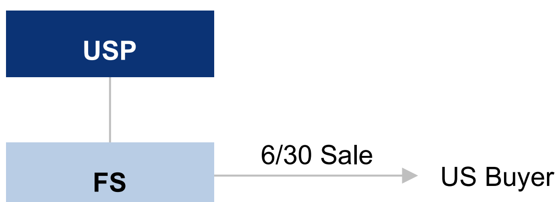
The Act significantly modifies the pro rata share rules such that a US shareholder may have a Subpart F or NCTI pro rata share inclusion if it owns stock of a CFC on any day of the taxable year (i.e., regardless of whether such US shareholder owns stock of the CFC on the last day of the year on which the corporation is a CFC). Under the Act, a US shareholder’s pro rata share is the amount of applicable CFC income that is attributable to the stock owned directly or indirectly by such US shareholder during the period of the CFC year in which such US shareholder was a US shareholder of such CFC.

However, the Act leaves it to regulatory authority to provide guidance on determining the income attributable to such US shareholder’s ownership, for example, in the case of a mid-year ownership change. The change is effective for taxable years of foreign corporations beginning after December 31, 2025.

Observations:

While regulatory guidance is necessary to understand how the pro rata share rules will work with mid-year changes, the new pro rata share rules will likely impact the allocation of responsibility for Subpart F and NCTI (formerly known as GILTI) inclusions in cross-border M&A deals. The changes will need to be factored into negotiations over issues such as Section 338 elections, post-close restrictions on actions, purchase price adjustments, and tax indemnities.

Figure 2: Example of Change in Pro Rata Share Rule



Transaction Description
On June 30, USP sells to US Buyer 100% of the equity interests in FS. FS is treated as a CFC both before and after the sale, and no election is made to close FS’s tax year. Each party uses the calendar year.

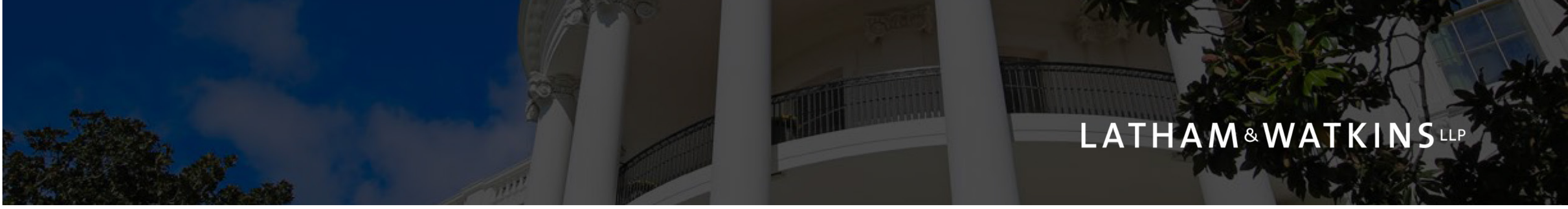
Old Law
Despite USP owning FS for half the year, USP would not be required to include any portion of FS’s Subpart F and net CFC tested income (f/k/a/ GILTI) in taxable income because USP would not own FS on the last day of the year on which FS is treated as a CFC.

New Law
USP would now have to include a pro rata share of FS’s Subpart F and net CFC tested income (f/k/a/ GILTI) in its taxable income. Inclusions under Section 956, however, would still be based on any US shareholders who hold stock on the last day of the taxable year.

C. Changes to GILTI; Renamed as NCTI

The GILTI rules can require a US shareholder of a CFC to include a GILTI inclusion in income, regardless of whether the income has been repatriated to the US shareholder.

Prior to the Act, domestic corporations were entitled under Section 250 to a 50% deduction on GILTI inclusions, but this deduction percentage was set to decrease to 37.5% in tax years beginning after December 31, 2025. The 50% deduction effectively reduced the effective tax rate on GILTI inclusions to 10.5% instead of the 21% corporate rate.



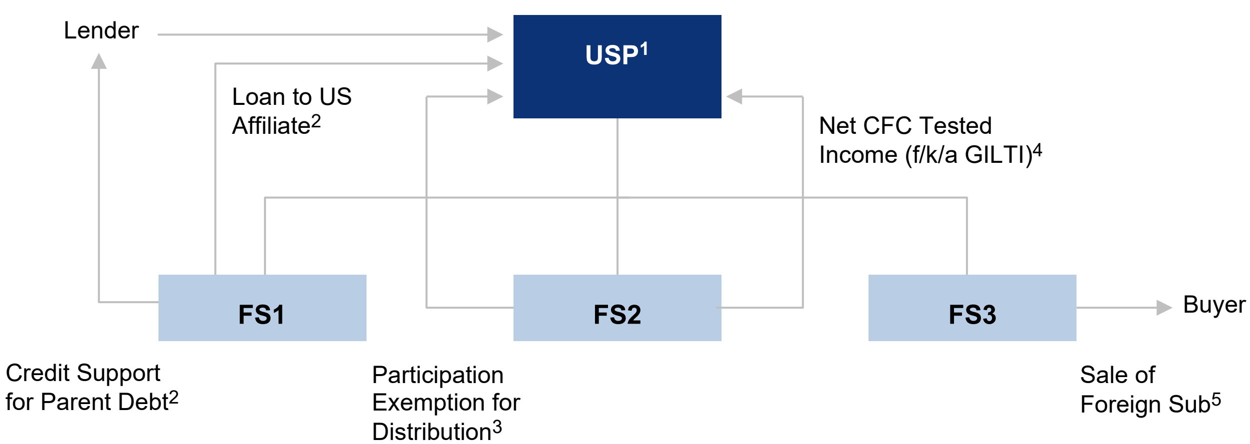
The Act makes permanent a 40% deduction for net CFC tested income inclusions that is applicable to tax years beginning after December 31, 2025. The 40% deduction essentially reduces the effective tax rate on this income to approximately 12.6% instead of the 21% corporate rate.

Under the TCJA, the GILTI inclusion was calculated by taking the CFC's tested income and subtracting a deemed tangible income return equal to 10% of the CFC's qualified business asset investment. This mechanism was designed to provide a tax-free return on tangible assets and subject only the excess return (presumed to derive from intangible assets) to US taxation.

The Act fundamentally restructures the GILTI regime by eliminating the deemed tangible income return concept. A US shareholder now includes in its income (as net CFC tested income or NCTI) its aggregate pro rata share of the tested income of its CFCs reduced by its aggregate pro rata share of the tested losses of its CFCs. References in the Code to global intangible low-taxed income or GILTI have been replaced with net CFC tested income or NCTI.

The deemed paid credit discussed in Part V.E, may result in no US tax on this income if the CFC that produces this income pays foreign income taxes at an effective rate of at least 14%.

Figure 3: Overview of International US Tax System



1 US Corporate tax rate remains at 21%.

2 Foreign subsidiary credit support for US Parent debt, or loans to US Affiliates, potentially taxed at 21%, less participation exemption and FTC (for non-exempt portion).

3 Dividends received deduction for 100% of qualifying distributions (the participation exemption).

4 Net CFC tested income (f/k/a/ GILTI) taxed at 12.6% rate, less FTC.

5 Participation exemption to extent of Section 1248 (dividend) characterization. Same rule applies on sale of lower-tier CFCs.

D. FTC: Deduction Allocations

The foreign tax credit (FTC) limitation under Section 904 is intended to limit the amount of the FTC to the amount of US tax that would otherwise be imposed on a taxpayer's foreign-source income. This limitation is generally calculated by multiplying the taxpayer's total US tax on worldwide income by a fraction — the numerator of which is the taxpayer's foreign-source taxable income and the denominator of which is the taxpayer's worldwide taxable income. The limitation is calculated separately for different categories of income, and one such category of income is NCTI (formerly known as GILTI). Expenses are required to be allocated and apportioned between US-source taxable income and foreign-source taxable income when calculating the FTC limitation fraction. The expense allocation can have a material impact on the FTC by effectively reducing foreign source income in the calculation of the FTC limitation.

The Act modifies the allocation and apportionment of deductions related to the NCTI category, effective for taxable years beginning after December 31, 2025. Modifications include limiting the allocation of interest expense and R&E expenditures of US-parented multinational groups to CFCs. The amendments are highly technical and complex, but, generally speaking, likely will result in limiting deductions allocable to the NCTI category, thus increasing the FTC limitation in the NCTI category.

E. FTC: Changes to Deemed Paid Credit

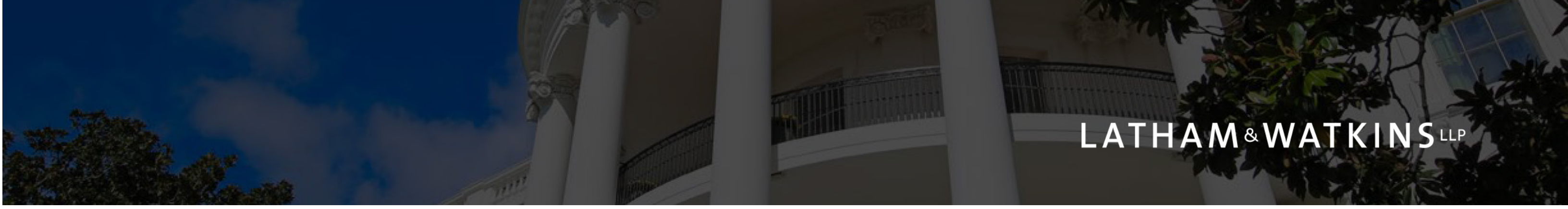
Under Section 960(d), for FTC purposes a corporate US shareholder is deemed to have paid certain foreign income taxes that were actually paid or accrued by a CFC, and that are properly attributable to income that is taken into account by the US shareholder when determining its NCTI (formerly known as GILTI) inclusion. The deemed paid amount is subject to certain limitations, and under the TCJA only 80% of the foreign income taxes attributable to the US shareholder's inclusion would be deemed paid (and FTC eligible) by the US shareholder. The Act increases this percentage from 80% to 90%, effective for taxable years beginning after December 31, 2025.

The Act also disallows FTCs for 10% of any foreign income taxes treated as paid or accrued with respect to any amount of income excluded from gross income under Section 959(a) by reason of a prior NCTI inclusion, which is applicable to NCTI inclusions after June 28, 2025.

F. FTC: Sourcing Inventory Sales

Under prior law, income from the sale of inventory produced in the United States would be sourced solely on the basis of the production activities with respect to the property. Inventory manufactured in the United States but sold abroad would, therefore, be sourced entirely to the United States.

The Act establishes a new sourcing rule solely for purposes of the FTC limitation (discussed in Part V.D), effective for taxable years beginning after December 31, 2025. Under the new sourcing rule, up to 50% of income from US-produced inventory sales that are attributable to the seller's foreign offices or fixed places of business are treated as foreign source income.



G. Changes to FDII Deduction

Under prior law, a domestic corporation was allowed a deduction equal to 37.5% of its foreign derived intangible income (FDII), but the deduction percentage was set to decrease to 21.875% for tax years beginning after December 31, 2025.

The Act makes permanent a 33.34% deduction for tax years beginning after December 31, 2025, and also makes certain changes to how FDII is determined. The 33.34% deduction essentially reduces the effective tax rate on this income to approximately 14% instead of the 21% corporate rate.

H. Changes to BEAT Tax Rate

The base erosion and anti-abuse tax (BEAT) under IRC Section 59A imposes an additional tax on certain large corporate taxpayers that make “base erosion payments” to certain foreign related persons. Prior to enactment of the Act, the BEAT tax rate was 10%, but it was scheduled to increase to 12.5% for tax years beginning after calendar year 2025.

The Act makes permanent a 10.5% BEAT tax rate for tax years beginning after December 31, 2025.

I. Look-Through Rule for Related CFCs Permanently Extended

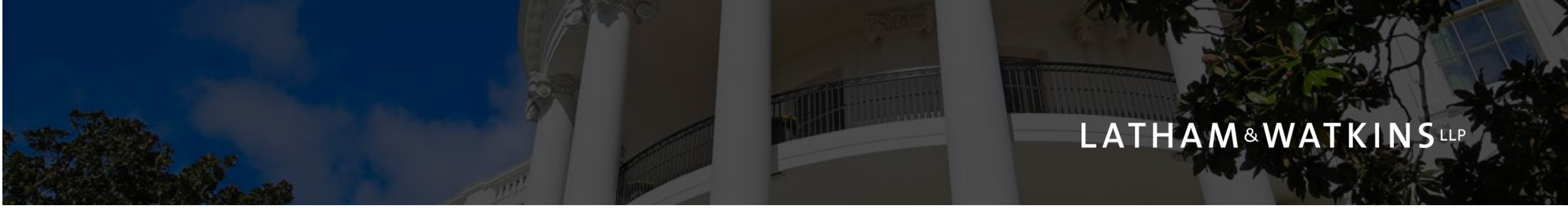
A look-through rule in Section 954(c)(6) allows dividends, interest, rents, and royalties received from a related CFC to be excluded from foreign personal holding company income (Subpart F income) if paid out of earnings that are neither Subpart F income nor income that is effectively connected with a US trade or business, but this was set to expire for tax years of foreign corporations beginning on or after January 1, 2026. The Act permanently extends application of the look-through rule.

J. Election for One-Month Deferral in Determination of Taxable Year Repealed

Under Section 898, CFCs that are majority owned by a single US shareholder are generally required to follow the tax year of their majority US shareholder. An election, however, was available for such CFCs to use a tax year beginning one month earlier than the majority US shareholder’s tax year. The Act repeals this election, subject to a special transition rule.

K. Excise Tax on Certain Remittance Transfers

The Act creates a new 1% excise tax on certain remittance transfers from senders located within the United States to recipients located outside of the United States, effective for transfers made after December 31, 2025. The tax applies exclusively to transfers where the sender provides physical payment instruments, including cash, money orders, cashier’s checks, and certain other similar physical instruments. Certain exceptions apply for physical payments that can be sourced to US bank accounts or US debit or credit cards.



VI. Qualified Opportunity Zones Extension and Enhancement

The Act establishes a permanent and enhanced Qualified Opportunity Zones (QOZ) program. QOZs were originally created under the TCJA to encourage investment in undercapitalized communities through tax incentives, but QOZs were originally scheduled to expire for new investments at the end of 2026 and the associated tax incentives were subject to several sunset provisions. The Act removes this expiration date and creates a new (and permanent) recurring redesignation cycle that starts on July 1, 2026, and repeats every 10 years. The Act also makes significant changes to the tax incentives available for investments in QOZs, including:

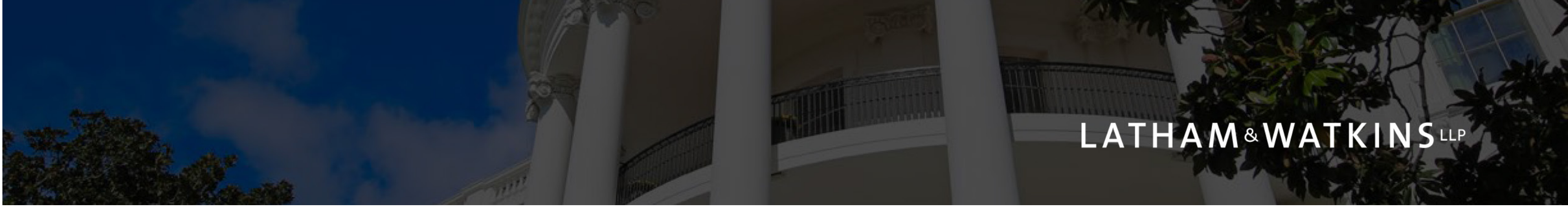
- **Extension of Gain Deferral Rules.** The Act provides a five-year deferral for certain gains (other than ordinary gains) that are reinvested after December 31, 2026, into Qualified Opportunity Funds (QOF) (generally, funds that invest in QOZs), or, if the investment is sold or exchanged in such five-year period, until the date of the sale. Under prior law, a taxpayer could similarly elect to defer recognition of gains reinvested into QOFs, but the deferral period was limited to December 31, 2026, regardless of the date of investment.
- **Changes to Partial Gain Elimination Rules**. The Act provides a partial elimination of gain (through a step up in tax basis) on certain investments in QOFs and an enhanced benefit for certain investments in newly created Qualified Rural Opportunity Funds (QROF) (generally, funds that invest in rural QOZs). If a taxpayer reinvests gain into a QOF after December 31, 2026, and holds that investment for at least five years, then 10% of the deferred gain (30% in the case of a QROF) can be eliminated through a tax basis step up. Under prior law, partial gain elimination was only available for investments in QOFs that were held for at least five years before December 31, 2026.
- **Extension of Complete Gain Elimination.** The Act provides that a taxpayer who holds its QOF investment for at least 10 years may elect on the disposition of its QOF investment to adjust the tax basis of the disposed investment to its fair market value on the earlier of the date of sale or the 30th anniversary of the investment date. Under prior law, the gain elimination was only available through December 31, 2047.

VII. Qualified Small Business Stock Enhancements

The Act makes significant amendments to Section 1202, which governs the QSBS gain exclusion, the primary purpose of which is to encourage investments in small, domestic businesses held in corporate form. Under prior law, a taxpayer's total aggregate excludable gain from QSBS issued by a single corporation was capped at the greater of $10 million or 10 times the taxpayer's aggregate adjusted basis in the disposed QSBS. Taxpayers were generally required to hold QSBS for more than five years to benefit from the QSBS exclusion; if the holding period was not satisfied, taxpayers would not be entitled to any QSBS exclusion. In order for stock issued by a corporation to constitute QSBS, the aggregate gross assets of the corporation must not have exceeded $50 million at any time before (and immediately following) the relevant stock issuance.

The Act increases certain dollar value thresholds in the QSBS rules (indexing these thresholds for inflation going forward) and softens the effect of the five-year holding period "cliff" for QSBS qualification. More specifically, the Act makes the following changes that are applicable to QSBS with an acquisition date on or after July 4, 2025 (the applicable date):

- **Increases the amount of gain a taxpayer can exclude per issuer of QSBS.** The Act raises the statutory dollar cap from $10 million to $15 million, indexed for inflation, and the alternative limitation — 10 times the taxpayer's aggregate adjusted basis in the QSBS — remains unchanged (providing a continued, alternative benefit for investors with significant adjusted tax basis in the stock). If a taxpayer exceeds the applicable QSBS gain exclusion, the taxpayer will no longer benefit from future inflation indexing, even if the taxpayer continues to hold QSBS issued by the applicable corporation (i.e., inflation indexing increases existing exclusions but does not create a new exclusion once the exclusion has been used in full).
- **Introduces a tiered, or phased in, gain exclusion based on the taxpayer's holding period.** Taxpayers will be eligible for the QSBS gain exclusion at a rate of 50% if the relevant stock is held for at least three years, 75% if the stock is held for at least four years, and the full 100% if the stock is held for five years or more. Under prior law, the gain exclusion was fully available for QSBS held for more than five years but unavailable for shorter holding periods. This change does not impact taxpayers who hold their QSBS for five years or more, but it provides a benefit for taxpayers selling QSBS after three or four years.
- **Broadens the definition of a "qualified small business."** The Act increases the aggregate gross assets test ceiling from $50 million to $75 million (generally, based on the adjusted tax basis of the corporation's assets). To qualify for QSBS treatment, a corporation's aggregate gross assets must not have exceeded this limit at any time prior to (and immediately after) the issuance of the stock in question. This 50% increase in the asset ceiling significantly expands the pool of corporations that may issue QSBS. Like the gain exclusion cap, the new $75 million threshold will be indexed for inflation beginning in 2027.
- **Continues treatment of gain excluded under Section 1202 as not a preference item for purposes of the alternative minimum tax (AMT).** An AMT preference item must be included in alternative minimum taxable income, even if the preference item is otherwise tax-free or tax deductible. This provision of the Act preserves an enhancement made to the QSBS regime in 2010 and ensures that the QSBS benefit is not partially negated through the application of the AMT.

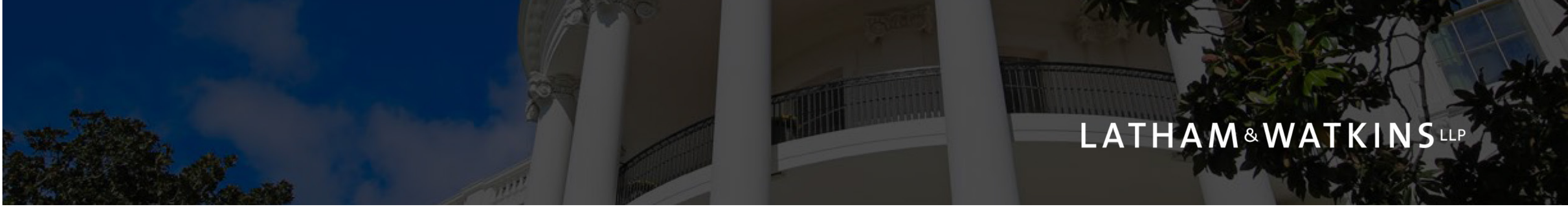


Summary of QSBS Changes

	Pre-Act Law (Stock Acquired on or Before July 4, 2025)	As Amended by the Act (Stock Acquired After July 4, 2025)
Per-Issuer Gain Cap	The greater of $10 million or 10 times the taxpayer's aggregate adjusted basis in the stock.	The greater of $15 million, indexed for inflation for taxable years beginning after 2026, or 10 times the taxpayer's aggregate adjusted basis in the stock.
Holding Period	Requires holding stock for more than five years for a 100% exclusion. A sale before this cliff results in a 0% exclusion.	Introduces a tiered exclusion: 50% for stock held at least three years, 75% for four years, and 100% after five years.
Aggregate Gross Assets Test	The corporation’s aggregate gross assets must not exceed $50 million at any time before and immediately after the stock issuance. R&E expenses must be capitalized.	The corporation’s aggregate gross assets must not exceed $75 million at any time before and immediately after the stock issuance, indexed for inflation for taxable years beginning after 2026. R&E expenses can be deducted.

Observations:

- The new tiered gain exclusion system provides taxpayers with QSBS more flexibility on exit timing, while still allowing some benefit from QSBS treatment.
- As noted above, these changes generally do not apply to QSBS initially issued on or prior to the applicable date. In addition, these changes generally will not apply to QSBS issued after the applicable date in exchange for QSBS issued on or prior to the applicable date.
- As discussed in Part II and Part III, the Act permanently reinstates 100% first-year bonus depreciation for qualifying property and the expensing of domestic R&E expenditures. These expensing provisions allow a company to immediately deduct rather than capitalize the cost of certain expenditures, which allows a company to avoid increasing its aggregate gross asset value (which is generally measured using adjusted tax basis) for QSBS purposes. The increase of the threshold for the aggregate gross assets test to $75 million and the change to bonus depreciation and R&E expensing, operating together, significantly expand the availability of the QSBS benefit, especially for businesses with extensive capital investments and research and experimental costs. Any corporation that intends to issue QSBS and is considering making the elections discussed in Part II and Part III (to take reduced first-year depreciation or to amortize domestic R&E expenditures) should consider whether these elections may cause the corporation to exceed the $75 million aggregate gross assets limit.



VIII. Individual Tax Changes

A. Extension of Individual Tax Rates

The Act makes permanent the lower tax rates and wider income brackets, which were set to expire at the end of 2025 under the TCJA. For example, the top marginal individual income tax rate remains at 37% rather than reverting to the pre-TCJA rate of 39.6% and the income brackets remain slightly wider than their pre-TCJA counterparts.

B. Increases to the SALT Cap; No Limitation on PTET Election

The Act temporarily increases the cap on the deduction for state and local taxes (SALT) to $40,000 (from $10,000) for households earning $500,000 or less beginning in 2025, and further increases both the cap and income threshold by 1% each year until the cap reverts to $10,000 starting in 2030.

Observations:

Since the enactment of the original SALT deduction cap in the TCJA, many states have enacted legislation that allows a passthrough entity to elect (a PTET Election) to pay an entity-level state tax (which is not subject to the SALT cap) in return for a credit or deduction against a state tax imposed on the owner of such passthrough entity, as a workaround to the SALT deduction cap. Notably, the Act does not include limitations on PTET Elections, though earlier versions of the bill had placed limitations on this workaround.

C. Limitation on Excess Business Losses Made Permanent

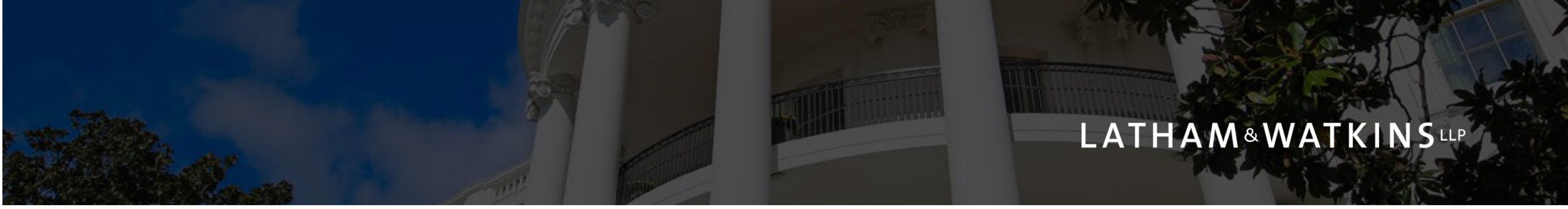
The Act makes permanent the disallowance of the deduction for excess business losses of noncorporate taxpayers, which was introduced by the TCJA and set to expire at the end of 2028. Excess business losses are the excess of the deductions attributable to the taxpayer's trades or businesses over the sum of (i) the taxpayer's aggregate gross income or gain attributable to such trades or businesses plus (ii) an inflation-adjusted annual threshold amount. The Act maintains the treatment of excess business losses as an NOL for the taxable year for purposes of determining the NOL carryover in subsequent years.

D. Disallowance of Miscellaneous Itemized Deductions Made Permanent

The Act makes permanent the disallowance of miscellaneous itemized deductions, which generally include deductions relating to management fees paid by individuals to investment funds. Such disallowance of deductions may limit the attractiveness of investment funds to high-net-worth individuals.

E. Itemized Deductions Phase-Out Made Permanent

The Act makes permanent an itemized deduction phase-out for high-income taxpayers. Under the phase-out, the maximum benefit of each $1 of itemized deductions is generally reduced from $0.37 to $0.35. The phase-out does not apply to the deduction for QBI discussed in Part I.A.



IX. Specific Taxpayer and Industry Impacts

A. Renewable Energy

Latham & Watkins published a Client Alert analyzing the impact of the Act on clean energy investment, which is available here.

B. Real Estate Investment Trusts

The Act increases the limitation on the percentage of a real estate investment trust's (REIT's) total assets that may be represented by securities of taxable REIT subsidiaries from 20% to 25% for taxable years beginning after December 31, 2025. This change provides REITs with greater flexibility to engage in activities beyond passive real estate ownership and facilitates more efficient structuring and operations through interests in taxable REIT subsidiaries without jeopardizing REIT status.

C. Publicly Traded Partnerships and Master Limited Partnerships; Expansion of Qualifying Income

Publicly traded partnerships (PTPs), including master limited partnerships (MLPs), must meet a 90% "qualifying income exception" in order to be classified as a partnership under the Code.

The Act broadens the definition of "qualifying income" for taxable years starting after December 31, 2025. This expanded definition now includes income and gains derived from:

- the transportation or storage of certain alcohol fuels, biofuels, sustainable aviation fuel, liquefied hydrogen, and compressed hydrogen;
- the generation and storage of electricity or the capture of carbon dioxide by certain qualified facilities;
- the production of electricity from certain advanced nuclear facilities;
- the production of electricity or thermal energy using geothermal energy or certain hydropower production; and
- the operation of certain geothermal energy property.

These additional sources of qualifying income are designed to expand the range of emerging energy technologies that can be funded through public equity offerings, thereby deepening the pool of available capital necessary to grow new energy infrastructure in the United States.

D. Oil and Gas Taxation; IDCs Excluded From Corporate Alternative Minimum Tax

The Act provides a new Corporate Alternative Minimum tax (CAMT) benefit to taxpayers with intangible drilling costs (IDCs). The CAMT is a minimum tax that is imposed on corporations with a three-year average Adjusted Financial Statement Income (AFSI) in excess of $1 billion. The CAMT is imposed at the rate of 15% of a corporation's AFSI, which is generally a corporation's net income or loss as determined in accordance with Generally Accepted Accounting Principles (GAAP), adjusted for certain items. For taxable years beginning after December 31, 2025, the Act may accelerate the expensing of IDCs for AFSI purposes by modifying AFSI to allow a reduction for certain IDCs that are deductible for tax purposes but required to be capitalized for GAAP purposes. Such IDCs may generally include expenses incurred by an operator in the development of oil and gas properties, such as wages, fuel, repairs, hauling, and supplies necessary for drilling wells and preparing them for oil or gas production. If a corporation's net income or loss (as determined by GAAP) includes depletion expense related to IDCs that were capitalized for GAAP purposes, it is disregarded for the AFSI calculation. This change may reduce the application and impact of the CAMT on taxpayers with IDCs.

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