Three Tax Issues Manufacturers Should Watch in 2025 Budget Bill

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On May 13, the House Ways and Means Committee voted to approve a $3.8 trillion tax bill that would make permanent much of the 2017 Tax Cuts and Jobs Act. The bill then moved to the House Budget Committee, where it was merged with other House Committee budget reconciliation bills to become the One Big, Beautiful Bill Act. On May 18, the House Budget Committee voted to advance the bill.

As Congress begins debating the bill's substance, manufacturing companies should be closely watching key industry items that are placed on the chopping block. Three areas that could be ripe for change are bonus depreciation, the qualified business income deduction and energy tax credits. Changes in each of these areas potentially have major implications for manufacturers nationwide.

Bonus Depreciation

Various iterations of the bonus depreciation provisions have been included in the Internal Revenue Code for over 20 years, often changed by the political winds of the time. This was the case in 2017, when the Tax Cuts and Jobs Act was passed into law.

The TCJA reduced the corporate income tax rate from 35% to 21%. Significantly, it also included changes to Internal Revenue Code Section 168(k), or bonus depreciation.

Under Section 168(a), the costs of certain business assets, such as equipment and buildings, are required to be depreciated over time based on the life of the asset. Taxpayers are required to expense that cost over a three- to 40-year recovery period. However, under Section 168(k), taxpayers are allowed to report a percentage of the cost of certain qualified property as an expense in the first year, instead of spreading it over a longer recovery period.

Prior to the TCJA, bonus depreciation was set to phase down annually over several years. The TCJA expanded bonus depreciation to initially provide a 100% allowance and made it applicable to the

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cost of certain qualified new and used property, meaning the deduction was available to more taxpayers and more property. Under the TCJA, the bonus depreciation allowance is phased out, going down to 20% in 2026 and 0% in 2027.

For purposes of bonus depreciation, "qualifying property" generally means property that has a recovery period of 20 years or less, such as furniture, office equipment, technology equipment, agricultural equipment, and manufacturing machinery and equipment, among other property.

Given this broad definition of qualifying property, any change to the TCJA's phasedown will affect capital-intensive industries—like manufacturing—the most.

For example, if a manufacturing plant needs to replace $10 million of qualifying equipment each year, the company's tax benefit from the acquisition of that equipment in 2027 could range from $10 million to $0, depending on whether Congress reinstitutes the TCJA's 100% allowance or lets the bonus depreciation allowance expire altogether.

Because the bonus depreciation rules in Section 168(k) have a significant impact on a capital-intensive company's purchasing and investment decisions, those companies should be watching Congress closely over the next couple of months, as any new tax legislation will affect their company's financials going forward.

Specifically, given the makeup of both houses, it is very likely that Congress will reinstitute some version of the TCJA's bonus depreciation rules, potentially making the 100% allowance permanent this time. Accordingly, capital-intensive companies should be armed with cash—or the financing necessary—to take advantage of such legislation this year.

Qualified Business Income Deduction

The TCJA also added Section 199A to the tax code—the qualified business income deduction, or QBID. The QBID allows certain partnerships, S corporations and sole proprietorships to deduct up to 20% of their qualified business income, or the net amount of income, gain, deductions and losses, from a qualified trade or

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business.

Under the TCJA, the QBID expires at the end of 2025. If it does, manufacturing companies taxed as partnerships, S corporations and sole proprietorships could face a higher tax burden, making C corporations look more attractive. This is especially true if the newly converted C corporation might also qualify for other tax benefits like the Section 1202 gain exclusion.

Under Section 1202, shareholders of qualified small business stock—when meeting certain requirements, including a five-year holding period—are allowed to exclude from their gain up to $10 million or 10 times their initial investment in the C corporation on the sale of the stock.

Given these trade-offs in tax benefits and the need to encourage more U.S. manufacturing—a stated goal of the current administration—it will be interesting to see how Congress reconciles its need to pay for new changes to the tax code. With that said, it's possible that the current Congress is likely to extend—or potentially make permanent—the TCJA's QBID. Anything else would be a tax increase on small business owners, the backbone of the U.S. economy.

Energy Tax Credits

Passed by Congress in 2022, the Inflation Reduction Act offered several tax credits designed to support U.S. manufacturing, particularly for companies involved in clean energy production, energy efficiency and reduction of carbon emissions.

A few of these credits include:

- The advanced manufacturing production credit, providing a per-unit tax credit for manufacturers producing components for clean energy—such as solar panels, batteries and wind turbines—for each eligible product made in the U.S.;
- The advanced energy project credit, providing a 30% tax credit on project costs for eligible manufacturers expanding or building facilities to produce solar panels, wind turbines, batteries, electric vehicles, carbon capture equipment and

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grid modernization components; and

- The clean hydrogen production credit, providing a production or investment tax credit from $0.60 to $3 per kilogram of hydrogen, depending on the carbon intensity of production, for eligible manufacturers with facilities producing hydrogen with low or zero emissions.

While there are many supporters of these credits in Congress, the current administration has been critical of these incentives, as many see the Inflation Reduction Act as a major contributor to the recent inflation.

Time will tell, but it is likely that these energy tax credits will be substantially reduced or rescinded entirely, as Congress will need to generate revenue to offset its other changes to the tax code, and these energy tax credits are not high on the current administration's priority list.

Conclusion

Manufacturing companies should keep a keen eye on the cuts Congress makes in the budget reconciliation that is ultimately passed. As Congress works to balance the satisfaction of its constituents, the current administration's agenda and the economy, manufacturing companies should anticipate changes such as those outlined above that will have a significant impact on capital-intensive industries. And with Congress' stated goal of passing a budget reconciliation bill by Memorial Day, these changes could be happening quite soon.

For more information regarding the proposed budget bill and its tax implications for manufacturers, please contact the authors or any attorney with Frost Brown Todd's Manufacturing Industry Team.

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Presidential Administration Impacts

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