AMERICANS FOR TaxFairness

"BONUS DEPRECIATION" OFFERS CORPORATIONS AN EXTRA CHANCE TO DODGE THEIR TAXES

"Bonus depreciation" was a temporary tax break enacted in 2002 and 2008 to stimulate the economy during recessions. Since 2008 it has been renewed as part of the package of tax extenders, which expired at the end of 2014. Bonus depreciation is an accounting maneuver that lets corporations write off the cost of big-ticket purchases much faster than they actually wear out, artificially inflating companies' costs and as a result, shrinking their tax bill. Even though studies show bonus depreciation doesn't help the economy much and whatever effect it does have hinges on being temporary, there are efforts underway to make the loophole permanent. The tax break's 10-year cost is $281 billion.

APPRECIATING DEPRECIATION AND THE PERMANENT MISTAKE OF BONUS DEPRECIATION

Businesses are allowed to deduct costs from income before figuring their taxes. Traditionally, only "operating expenses"—the cost of goods or services that get used up right away, like salaries, supplies and utilities—can be deducted in their entirety the year they're incurred. "Capital expenses"—long-term investments like manufacturing equipment—must be deducted ("depreciated") slowly over time, to reflect their continued usefulness and slow loss of value. The more a corporation can deduct from its income, the smaller its tax bill.

"Bonus depreciation" allows businesses to deduct a large part—sometimes all—of a capital expenditure at the time of purchase. The most recent form of bonus deprecation included in tax extenders legislation allowed 50% of the cost of equipment purchased to be deducted immediately.[1] The House Ways and Means Committee recently approved making permanent an expanded form of bonus depreciation,[2] which would cost $281 billion over 10 years.[3] Bonus depreciation was supposed to be temporary. It was included in economic stimulus packages enacted to fight the last two recessions in 2002 and 2008.[4] The purpose was to boost the economy by encouraging businesses to spend money sooner (during the period of the tax break) rather than later (after it had expired). Making the loophole permanent eliminates whatever stimulating effect a temporary version has, since companies won't be moving up their investments to beat a deadline. It becomes just one more corporate tax giveaway.

BONUS DEPRECIATION IS MORE THAN A BONUS—IT'S AN UNWARRANTED GIFT

Tax deductions are supposed to relate realistically to business expenditures. When a company pays a salary or an electric bill, buys raw materials for its factory or food for its cafeteria, all the expense occurs immediately (or nearly so). But if it buys a blast furnace or fleet of trucks, those investments don't get used up in the year of purchase—they last and continue to produce income for years to come. So it makes no sense for the whole cost—rather than a small portion of it—to be deducted that first year.

The Congressional Research Service examined numerous academic studies and concluded that "temporary accelerated depreciation is largely ineffective as a policy tool for economic stimulus. … Furthermore, there is anecdotal evidence that the current bonus depreciation allowance has made little or no difference in the investment plans of some companies, while accelerating the timing of planned investments by other companies to take advantage of the tax savings."[5] In other words, businesses would have invested even without bonus depreciation. Renewing this tax break to cover investments already made in 2015 would be a pure handout since, by definition, an incentive can't be retroactive.[6]

Even if Congress wanted to stimulate the economy at this time of steady growth and low unemployment, bonus depreciation is a very inefficient remedy. Moody's Analytics found that the bang for the buck (additional GDP per tax dollar) of accelerated depreciation, which is similar to bonus depreciation, is much less effective than other types of tax cuts or public spending. For example, every dollar "spent" on depreciation creates just 29 cents of economic activity vs $1.23 for the Earned Income Tax Credit, $1.38 for the Child Tax Credit, $1.44 for infrastructure investment and $1.70 for Food Stamps spending.[7]

CASE STUDY: BONUS DEPRECIATION POWERS NEGATIVE TAX BILL

Corporations with heavy capital investments—like utilities—benefit particularly from bonus depreciation. Pacific Gas and Electric (PG&E), a huge California power company, has used the accelerated write-offs of bonus depreciation to avoid paying any federal income taxes from 2008 through 2014.[8] In fact, despite $10 billion in profits over that span, the utility received an astonishing $1.5 billion in federal tax refunds, for an effective U.S. tax rate of *negative* 15%.

Big corporations already dodge taxes—bonus depreciation allows them to contribute even less to our national finances. With highways and bridges deteriorating,[9] kids being excluded from preschool[10] and the retirement prospects for most Americans looking dire,[11] it is not the time to give one more tax break to profitable corporations. Instead, we should be demanding that corporations pay their fair share. Bonus depreciation is a big minus for the American people.

ENDNOTES

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[1] Congressional Research Service (CRS), "The Section 179 and Bonus Depreciation Expensing Allowances: Current Law and Issues for the 114th Congress" (August 6, 2015), p. 3. http://nationalaglawcenter.org/wp-content/uploads/assets/crs/RL31852.pdf

[2] House Ways and Means Committee, "H.R.2510 - To amend the Internal Revenue Code of 1986 to modify and make permanent bonus depreciation." The legislation was reported out of the committee on October 28, 2015. https://www.congress.gov/bill/114th-congress/house-bill/2510

[3] Joint Committee on Taxation, "Description Of An Amendment In The Nature Of A Substitute To The Provisions Of H.R. 2510, A Bill To Modify And Make Permanent Bonus Depreciation" (September 16, 2015). https://www.jct.gov/publications.html?func=startdown&id=4829

[4] CRS, "Using Business Tax Cuts to Stimulate the Economy," (Jan. 18, 2013), Summary. https://www.fas.org/sgp/crs/misc/RL31134.pdf

[5] CRS, "The Section 179 and Bonus Depreciation," pp. 12-14. See also CRS, "Bonus Depreciation: Economic and Budgetary Issues" (July 7, 2014), pp. 5-7. https://www.fas.org/sgp/crs/misc/R43432.pdf

[6] CRS, "Bonus Depreciation: Economic and Budgetary Issues," p. 4.

[7] Moody's Analytics, "An Analysis of the Obama Jobs Plan" (September 9, 2011), Table 3. https://www.economy.com/dismal/analysis/free/224641

[8] Citizens for Tax Justice, "A 'Tax Extenders' Provision Has Allowed Highly Profitable PG&E to Pay Zero Taxes the Last Seven Years" (February 20, 2015). http://www.taxjusticeblog.org/archive/2015/02/a_tax_extenders_provision_has.php#.VktJiHiHbNq

[9] American Society of Civil Engineers, "2013 Report Card for America's Infrastructure." http://www.infrastructurereportcard.org/executive-summary/

[10] Coalition on Human Needs, "Selected Human Needs Programs: Shrinking Funding Since 2010" (Mar. 9, 2015). http://www.chn.org/wp-content/uploads/2015/01/Shrinking-Funding-Since-2010-Approps-FY10-FY15-1.30.15.pdf

[11] Center for Effective Government and the Institute for Policy Studies, "A Tale of Two Retirements" (October 28, 2015). http://www.foreffectivegov.org/two-retirements