REFUNDABLE BUSINESS TAX CREDITS ARE A COSTLY GIVEAWAY TO BIG FIRMS & DON'T BELONG IN THE NEXT CORONAVIRUS AID BILL

Corporate lobbyists are pushing Congress to include in the next coronavirus relief package a provision to make business tax credits refundable. That would mean firms with credits that exceed their tax liabilities in a given year could get a refund that year, rather than being forced to carry the credits forward to reduce tax liabilities in future years. Refundable business tax credits are a bad idea both on general policy grounds and for reasons specific to the proposal.

GENERAL ARGUMENTS AGAINST BUSINESS TAX BREAKS

Business tax cuts are an unfocused relief measure that make no demands on the recipients. Unlike targeted forms of economic relief like the "Paycheck Protection Program (PPP)," business tax cuts give cash to large corporations and business owners without any requirement that they maintain payroll or make other socially useful investments. That cash could instead be used simply to reward their wealthy shareholders with higher dividends and stock buybacks, as corporations did with their savings from the 2017 Trump-GOP tax law. Making already rich CEOs and other big shareholders even richer does nothing to lift the economy back up from its steepest fall since the Great Depression.

Tax breaks for corporations are an expensive, ineffective way to combat the pandemic recession. In a recent letter to Speaker Pelosi evaluating the effect on the economy of various forms of enacted coronavirus relief and stimulus, the CBO ranked business tax cuts behind aid to state and local governments and increases in federal spending on Medicare. This perspective is backed by research by eminent economist Mark Zandi of Moody's Analytics that he recently cited: business and investment tax cuts generally cost several times more than they generate in increased economic activity. This contrasts with spending on aid for needy families, the unemployed, or state and local governments, or on infrastructure spending, all of which generate much more economic activity than they cost.

Big businesses have already gotten too many tax cuts and don't need more. Businesses already received several hundred billion dollars in tax cuts in the most recent pandemic relief measure, the CARES Act, including the notorious "Millionaires Giveaway." That provision alone costs $135 billion and is giving a $1.6 million average tax cut to 43,000 millionaires this year. It is opposed by more than 230 organizations. In the 2017 tax overhaul, President Trump and Congressional Republicans handed corporations a tax cut of roughly $750 billion.

Corporate tax cuts, refundable or otherwise, don't help workers, despite claims to the contrary. The 2017 Trump-GOP business tax cuts were promised to increase the average household's wages by at least $4,000 (above any increases that would have happened without the tax law). Instead, median family income inched up just a little over $500 in the first year after the law was enacted—compared to an average yearly increase of more than $1,300 over the preceding five years—and real wage growth for rank-and-file workers continued to be slow through 2019. The rate of wage increases in the last two years of the Obama Administration was over three times that of the first two Trump years. If absolute cuts in tax rates and other new breaks for big business didn't benefit workers, it's unlikely a simple acceleration of existing credits would do much for them.

The 2017 Trump-GOP corporate tax cuts were supposed to spur investment, but even before the pandemic, that promise had proved false. Trump's top economic adviser said before the bill passed that he "would expect capital spending to really take off" if the Republican tax bill, which slashed the corporate tax rate by 40%, were enacted. Instead, after a mild spurt in early 2018, business investment actually fell into negative territory over the last three quarters of 2019, as corporations used their tax cuts to reward shareholders rather than invest.

SPECIFIC REASONS TO OPPOSE MAKING BUSINESS TAX CREDITS REFUNDABLE

Business tax credits are supposed to offset actual tax liabilities, not potential tax liabilities. Allowing businesses to use tax credits now, rather than when actual tax liabilities arise, is an unwarranted windfall. Taxes are only levied on profits. Since some businesses never become profitable, making a payment to a taxpayer based on taxes that will never be due is not so much an advance refund as a simple handout.

The most expensive business tax credit—for research and development—is already effectively refundable for small businesses, so the current proposal would only help big companies. The PATH Act of 2015 made several significant reforms to the research and development tax credit, including permitting qualified small businesses to apply the R&D credit against their payroll tax liability, essentially making it a refundable credit. So only bigger companies would benefit from the change proposed now—and they make heavy use of the R&D credit, making the current proposal potentially very expensive. According to the Joint Committee on Taxation's examination of tax expenditures (Table 1, p. 20, "Credit for increasing research activities"), over the five years 2019-23 more than 80% of the $70 billion value of the R&D tax credit will be taken by corporations, not individuals (who qualify by running so-called pass-through businesses such as sole proprietorships and partnerships).

Established businesses already have a way to monetize tax credits. The Federal Reserve, buoyed by the $454 billion provision in the CARES Act for Treasury's Exchange Stabilization Fund, has taken extraordinary measures to make sure credit would not dry up during this pandemic. Moreover, interest rates are at historic lows, allowing businesses to borrow cheaply; and stock prices are relatively high, richly rewarding businesses selling shares. As a result, corporations in need of liquidity can profitably access the capital markets directly or borrow cheaply against the value of their tax assets. Further Congressional action is not needed to let corporations tap the value of these credits. Congress ought to focus on helping the tens of millions of employed and unemployed workers and small business owners struggling through the pandemic, rather than further aiding stockholders who are doing relatively well.

Allowing businesses to take tax credits early, instead of making them wait to use them till they have enough tax liability to match them against, would encourage tax fraud. Refundable tax credits would incentivize the unscrupulous to create fraudulent businesses to claim those credits—businesses that would then disappear before a resource-constrained IRS could audit them. Thieves have already taken advantage of the CARES Act's PPP loan program by creating fake businesses. Creating an easy target for fraudsters in the form of refundable business tax credits would only add to the administrative burden of the IRS, which is already failing to investigate high-income households that don't even bother to file tax returns. Moreover, depending on the manner in which legislative language is structured, making credits refundable could facilitate the creation of tax shelters.