CTJ Citizens for Tax Justice

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Why Lawmakers Should Reject the Deficit-Financed $680 Billion Tax Cut Deal

Late Tuesday, congressional leaders announced the details of a $680 billion tax cut deal that will be up for a vote in the House and Senate over the next couple days. While there are some worthwhile provisions in the package, they come at too high a price to justify supporting the overall package.

The bulk of the tax cut package includes extending or making permanent many of the temporary tax provisions known as the tax extenders. The legislation also includes making expansions to the Child Tax Credit (CTC) and Earned Income Tax Credit (EITC) permanent, making the American Opportunity Tax Credit (AOTC) permanent, and delaying (or, in one case, eliminating for one year) three Obamacare-related taxes.

Here are the three reasons why lawmakers should reject this tax deal:

1. The deal will revive or make permanent ineffective tax breaks for business.
2. The deal will increase the deficit by $680 billion over the next ten years.
3. The tradeoff between the good and the bad provisions is not equitable and, due to deficit-financing, could ultimately threaten the well-being of low- and middle-income Americans by forcing draconian cuts to critical programs.

1. The deal will revive or make permanent ineffective tax breaks for business.

Most of the extenders are ineffective and do not serve the public interest. Of the more than 130 provisions, just six of the business provisions constitute nearly half of the total cost of the package. The cost of just two corporate provisions, the research credit and active financing exception (AFE), is $191 billion or 28 percent of the cost of the overall package.

As CTJ has noted time and again, the research credit should be substantially reformed or allowed to stay expired, not made permanent as is proposed in the tax deal. While the idea of encouraging research sounds good, in reality the research credit is a particularly poor way of pursuing this goal because it often subsidizes “research” of no public value or research that would have been done anyway.

Another particularly egregious provision is the extension of "bonus depreciation" for three years, allegedly to be followed by a phase-out of this loophole over three years. Bonus depreciation was originally adopted as a temporary stimulus measure early in the George W. Bush administration. It has been reenacted in almost every year since, despite the fact that the non-partisan Congressional Research Service called it "a relatively ineffective tool for stimulating the economy." With a 10-year cost of $246 billion, bonus depreciation is by far the most costly provision in the tax extenders. It has also been a key reason why many large, profitable corporations have paid little or nothing in income taxes for the past decade and a half. By extending this provision only for a few years, the break masks the long-term cost of its likely permanent extension. The fact that it will allegedly be phased out after three years may seem like a positive sign, but it should not be taken too seriously. After all, this means that bonus-depreciation advocates have another three years to make sure that this phase-out never happens.

Two of the other worst provisions of the tax deal are those that will make permanent the AFE and extend for five years the Controlled Foreign Corporation (CFC) Look-Thru Rule, at a combined cost of $86 billion over the next 10 years. Rather than working to counter the historic levels of offshore corporate tax avoidance, the extenders bill will enshrine into law two loopholes that have become central to enabling this bad behavior. If lawmakers are really concerned about combating offshore tax avoidance, a good place to start would be to allow these two provisions to remain expired.

While not as large, most of the other 50 tax extender provisions that will be extended or made permanent in the tax deal are also of dubious efficacy, as outlined in a recent CTJ report "Evaluating the Tax Extenders."

2. The deal will increase the deficit by $680 billion over the next ten years.

There is no way to get around the cold hard fact that the tax deal will add $680 billion to the nation's budget deficit over the next 10 years. In fact, this package will erase all of the revenue "raised" by the expiration of the Bush tax cuts for the wealthy as part of the Fiscal Cliff Package at the start of 2013.

The need for more revenue is absolutely critical. Even without making essential new public investments, the U.S. federal government already faces a $7 trillion budget hole over the next 10 years. It is ridiculous that Congress is now proposing to substantially expand this hole.

While some argue that we should consider the current slate of temporary tax provisions to be part of the budget baseline already, even anti-tax conservative lawmakers have admitted time and again that making the federal budget sustainable requires paying for these provisions. For example, both the current Republican Speaker of the House Paul Ryan and the former Republican Chairman of the Ways and Means Committee Dave Camp have advocated for a revenue baseline that would fully pay for the cost of the tax extenders and other temporary tax provisions. In other words, the principle of paying for these temporary tax provisions has neither been lost nor should it be given up.

3. The tradeoff between enacting good and bad provisions is neither equitable nor worth the cost.

One argument for supporting the overall tax deal is that the benefit of securing a permanent place in the tax code for the expansions in the EITC and CTC is worth the cost of passing the numerous and undesirable provisions in the package. While it might be worth some kind of tradeoff to secure the EITC and CTC expansions, the price being asked for in this deal is unacceptably high.

For every dollar spent in the deal on expanding the working families' tax credits, five more dollars are being spent on other tax cuts. The cost of the top six business provisions alone is 2.5 times the size of what is being spent on the EITC and CTC expansions in the package. Both the EITC and CTC are highly effective tax credits that should be made permanent on their own and should not require the passage of foolish and unfair tax breaks many times their size.
It is also important to note that if this package is enacted, the resulting higher budget deficits will, in the long run, threaten low-income programs including the welcome expansions of the EITC and CTC. In other words, the extenders package's deficit spending is not free, and it could come back to bite low-income programs in the future.