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CORPORATE AMT REPEAL IS INEFFECTIVE STIMULUS

by Joel Friedman

Despite attempts by the Administration to distinguish its proposal to repeal the corporate Alternative Minimum Tax from the widely-criticized House-passed provision, these two proposals are quite similar. Both shower benefits on profitable corporations but do little to generate new investment and thus stimulate the economy.

- The primary difference between the proposals is the timing of the benefits — under the House provision corporations would receive more of their tax break immediately, in the form of refund checks from the Treasury, while under the Administration's approach these corporations would receive their benefits over a longer period of time.

- As a result, the Joint Committee on Taxation estimates that the cost of these two proposals over ten years is basically the same — $24 billion for the House's proposal and $22 billion for the Administration's proposal.

Furthermore, under the Administration's approach, about 60 percent of the ten-year cost of repealing the corporate AMT would occur after 2002, in years when the economy is expected to have already recovered from the current recession. Thus, the proposal is not only ineffective at meeting the economy's short-term needs, but will worsen the long-term budget outlook. These long-term costs are particularly troubling given recent pronouncements by the Administration's Budget Director Mitchell Daniels that the fiscal forecast has deteriorated sharply and that the budget including Social Security will be in deficit through 2004.

The corporate AMT was originally implemented in response to actions by a number of large, highly profitable corporations to use tax breaks so aggressively that they largely or entirely escaped paying income tax. Its elimination would likely lead to a situation in which profitable corporations again escape the income tax.

Corporate AMT Does Not Promote New Investment

Repeal of the corporate AMT is poorly designed as a stimulus measure, providing no incentive to spur new business investment; but only new business investment is stimulative. In a recent analysis, Brookings Institution senior fellows William Gale and Peter Orszag estimate that in 2002, approximately 90 percent of the tax reductions from eliminating the corporate AMT would consist of tax cuts on profits from *old* investment — that is, investments made in years before 2002 — rather than new investment.[1] The Brookings analysis concludes that repealing the corporate AMT consequently would do little to provide short-term stimulus. Gale and Orszag observe that "elimination of the corporate alternative minimum tax is an extremely blunt and inefficient approach to encouraging new investment in the short run."

AMT Credits Flow to Corporations

The House-passed proposal to repeal the AMT was widely criticized for including a provision that would make existing corporate AMT credits "refundable," such that Treasury would write substantial refund checks to some of the country's largest and most profitable corporations. In an attempt to distinguish itself from the House plan, the Administration would allow these credits to be paid out "prospectively." Thus corporations would still receive the tax break, but over a longer period.

These credits essentially represent the amount of alternative minimum tax that corporations have paid in previous years. A corporation can use these credits only to offset regular corporate income tax in years that the income tax it owes exceeds the amount it would owe under the corporate AMT. Corporations that routinely pay the AMT (or that do not owe much in corporate income tax) thus are not able to make full use of these credits.

Under the House-passed provision that would make these credits "refundable," corporations would receive checks up-front for the value of their accumulated credits. According to the Citizens for Tax Justice, 16 corporations would receive checks of over $100 million each.[2] A report by the Congressional Research Service also identified a number of corporations that would receive sizable benefits.[3] For instance, both reports found that $1.4 billion would flow to IBM, $833 million to General Motors, and $671 million to General Electric.

While the Administration's provision would make not these credits "refundable," corporations would still be able to claim most of these credits in later years under the Administration's "prospective" approach. This is why there is little difference in cost over ten years between the two versions of corporate AMT repeal. Under the House corporate AMT provision, these corporations would gain $24 billion over ten years. Under the Administration's provision, these corporations would secure $22 billion in tax breaks over ten years. Thus the same corporations — such as IBM, General Motors and General Electric — that would benefit under the House bill would reap substantial benefits under the Administration's corporate AMT repeal proposal as well.

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[1] William Gale and Peter Orszag, "Evaluating President Bush's Tax Stimulus Package," Brookings Institution, October 9, 2001.

[2] Robert McIntyre, "House GOP 'Stimulus' Bill Offers 16 Large, Low-Tax Corporations $7.4 billion in Instant Tax Rebates," Citizens for Tax Justice, October 26, 2001 updated.

[3] Congressional Research Service, Memorandum to House Ways and Means Committee, "Corporate Alternative Minimum Tax for 50 Corporations," October 16, 2001.