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June 11, 2020

# Proposal to Extend Full Expensing Beyond 2022 Could Discourage Investment This Year and Hurt the Recovery

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In recent weeks, the Trump Administration[1] and some members of Congress[2] have proposed making permanent the 2017 tax law's "full expensing" provision, which allows businesses to reduce their tax liabilities by deducting the full cost of investments immediately rather than over a number of years. Current law *already* permits full expensing until the end of 2022, so making it permanent would have no effect until 2023 and hence do nothing to help mitigate the current economic downturn. If anything, by having the tax break remain available after 2022, the proposal could *discourage* business investment in the short run, which could make the ongoing economic downturn deeper and the recovery weaker.

Moreover, making full expensing permanent would cost roughly $190 billion through 2030. Those resources would be far better spent on more effective fiscal stimulus tools.

In past economic downturns, policymakers have tried to encourage businesses to make new investments or speed up planned future investments by allowing larger upfront tax deductions for these investments. These policies — generally referred to as "bonus depreciation," of which full expensing is the most aggressive variation — have not been particularly effective at boosting investment and stimulating the economy during a recession, when many businesses lack customers to purchase their goods and services or cash to make investments. For these reasons, the Congressional Research Service has stated that bonus depreciation provisions are generally a "relatively ineffective tool for stimulating the U.S. economy during periods of weak or negative growth."[3]

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[1] Erica Werner *et al.*, "Trump and Congress spar over next coronavirus economic package as CBO paints grim picture of what's to come," *Washington Post,* April 24, 2020, https://www.washingtonpost.com/us-policy/2020/04/24/trump-cbo-congress-coronavirus/.

[2] Alan K. Ota, "Rep. Neal Open to GOP Biz Expensing Plan for COVID-19 Bill," Law 360: Tax Authority, April 24, 2020, https://www.law360.com/tax-authority/federal/articles/1267310/rep-neal-open-to-gop-biz-expensing-plan-for-covid-19-bill.

[3] Gary Guenther, "The Section 179 and Section 168(k) Expensing Allowances: Current Law and Economic Effects," Congressional Research Service, May 1, 2018, https://fas.org/sgp/crs/misc/RL31852.pdf.

Effective economic stimulus helps shore up purchases of goods and services by getting resources quickly to businesses and households that are most likely to spend those resources, or getting cash to businesses that can't otherwise find a way to borrow. The biggest problem that businesses face as a result of the COVID-19 pandemic is the lack of customers for their goods and services. Some also lack enough cash to tide them over until social distancing measures ease and customers return. Broad-based business tax cuts, like extending full expensing, do little to help businesses with either of these problems. As a result, a large amount of the cost of such a provision would simply reflect a windfall tax cut to businesses and business owners that don't need it because they either would have made the investments anyway or will not make new investments more quickly now whether they get such a tax break or not.

As Congress considers additional COVID-19 relief and stimulus legislation, lawmakers should turn aside tax-cut proposals that would provide windfalls to owners of businesses that are weathering the crisis while doing little to shore up businesses that are struggling, increase demand for goods and services, or strengthen the economy overall.

## Bonus Depreciation Is Poor Stimulus

Periodically in recent decades, including during the Great Recession in 2008, Congress has enacted temporary "bonus depreciation" measures that allow businesses to take larger upfront tax deductions for equipment and other purchases than they can take under the regular depreciation rules (under which the cost of such purchases is deducted over a longer period of time depending on the useful life of the asset).[4] In theory, the temporary tax incentive is designed to encourage businesses to make investments they otherwise wouldn't make, or to speed up investments they planned to make in the future, with the hope that spending on these purchases will help stimulate a weak economy. Full expensing is the most aggressive variation of bonus depreciation, allowing businesses to deduct 100 percent of the cost of equipment in the year they buy it.

At best, bonus depreciation is costly, weak short-term stimulus. Bonus depreciation has fairly low "bang for the buck" as economic stimulus, analyses from Moody's Analytics[5] and the Congressional Budget Office[6] both show. For example, estimates from Mark Zandi of Moody's suggest that every $1 of tax revenue lost from bonus depreciation generates less than 30 cents in economic activity. That means that much of the money spent on such a provision is wasted on activity that would have happened anyway, sits idle in businesses coffers, or is passed on to business owners (who tend to be well off and therefore likely to save rather than spend any additional dollars they receive).[7]

This is because businesses are less likely to invest during economic downturns, "when they have idle capacity and when they are less confident about the future demand for their products and

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[4] For example, under the 2008 bonus depreciation rules, a business that invested $1 million in equipment could immediately deduct 50 percent of the cost, or $500,000, with the remaining cost depreciated under the normal rules for that asset.

[5] Mark Zandi, "Global Policy Prescriptions: How Another Recession Can Be Avoided," Moody's Analytics, August 26, 2011, https://www.economy.com/mark-zandi/documents/Policy-Prescriptions-20110826.pdf?src=DS.

[6] Douglas W. Elmendorf, "Policies for Increasing Economic Growth and Employment in 2012 and 2013," Congressional Budget Office, November 15, 2011, http://www.cbo.gov/sites/default/files/cbofiles/attachments/11-15-Outlook_Stimulus_Testimony.pdf.

[7] Zandi, *op. cit.*

services."[8] Simply making it cheaper to purchase equipment and other business assets will have little effect on business investment if businesses still lack customers to buy the products that such investments would produce.

And, while many businesses need an infusion of cash to remain viable until social distancing measures ease and consumer demand strengthens, expensing or bonus depreciation is poorly targeted for that purpose. The only businesses that can get the benefit of expensing or bonus depreciation are those that have the resources to purchase new equipment that qualifies for the expensing tax break. With or without the tax break, these businesses are likely already in a relatively stronger position to weather the crisis.

By contrast, the best stimulus measures go directly to cash-strapped households likely to spend any extra resources they receive, shoring up spending on a range of goods and services. This in turn helps businesses and workers who provide those goods and services to maintain their own spending. So, for example, increased spending on nutrition assistance through SNAP (food stamps) boosts a weak economy by about $1.50 for every dollar spent, researchers at the Agriculture Department's Economic Research Service have estimated.[9]

## Permanent Extension of Full Expensing Could Actually Worsen the Recession and Weaken the Recovery

The 2017 tax law enacted full expensing for most assets[10] through 2022, converting to gradually decreasing bonus depreciation from 2023 through 2026. Making the 2017 tax law's full expensing provision permanent would cost roughly $190 billion between 2023 and 2030.[11] But this costly policy is unlikely to encourage any new business investment and could even result in *delaying* such investment, thereby harming, rather than aiding, the recovery.

If expensing or bonus depreciation were enacted as a *temporary* measure during a downturn, it could induce some firms to accelerate purchases. Such a boost would be modest, at best, for the reasons discussed above. And any such small boost would stem from the fact that the extra tax break would apply *only* to purchases made during the temporary period that it is in effect.

Making the current tax break permanent, however, would give firms *no* incentive to accelerate purchases while the economy is faltering, because they already benefit from full expensing until 2023. In fact, allowing full expensing in 2023 and beyond could actually *discourage* business investment in the short term; if firms can reap the tax benefits of full expensing regardless of when

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[8] *Ibid.*

[9] Patrick Canning and Rosanna Mentzer Morrison, "Quantifying the Impact of SNAP Benefits on the U.S. Economy and Jobs," USDA, Economic Research Service, July 18, 2019, https://www.ers.usda.gov/amber-waves/2019/july/quantifying-the-impact-of-snap-benefits-on-the-us-economy-and-jobs/ .

[10] Certain types of assets, including buildings and other structures, may not be fully expensed and must instead be depreciated over a longer time period.

[11] CBPP analysis of CBO data. This analysis is based on data released prior to the COVID-19 outbreak and does not take into account changed post-pandemic economic conditions. Congressional Budget Office, "The Budget and Economic Outlook: 2019 to 2029," January 28, 2019, https://www.cbo.gov/publication/54918; Congressional Budget Office, "The Budget and Economic Outlook: 2020 to 2030," January 28, 2020, https://www.cbo.gov/publication/56073.

they make their investments, they are less likely to accelerate investments between now and 2022 to take advantage of the tax break. Given all of the uncertainties in the economic outlook, giving businesses another reason to hold off on investments could worsen the recession and prolong the recovery.

## Tax Sheltering Is Not Sound Stimulus

In addition, making full expensing permanent could expand tax sheltering opportunities — ways that profitable businesses can avoid tax while changing few if any of their hiring or investment practices. In particular, as a result of the combined effect of full expensing and other tax breaks, businesses that take out loans to buy equipment or other depreciable assets can essentially get a *double* tax benefit: a full deduction for the price of a purchased asset *and* deductions for interest on the debt used to buy that asset. According to New York University tax law professor Lily Batchelder,"[t]his is converting the tax code basically into a direct spending program for anything that people can get a tax lawyer to say is debt-financed business investment."[12]

This would be especially problematic if full expensing were extended to buildings, as the Trump Administration is reportedly considering.[13] That's because the real estate industry relies heavily on debt financing for building purchases and takes frequent advantage of the associated interest deductions. Allowing full expensing for buildings, while continuing to permit interest deductions,[14] would create vast new tax sheltering opportunities for profitable real estate developers.

## Policymakers Should Pursue Better Stimulus Options

Instead of providing businesses with a tax cut that won't significantly boost consumption during the economic downturn, policymakers should address immediate needs and problematic gaps in earlier relief measures.[15] For example, they should enact high-impact relief and stimulus measures such as aid to help state and local governments cover their massive revenue shortfalls and avoid deep cuts to services (which would deepen and prolong the recession).[16] They should also strengthen nutrition assistance;[17] supplement benefit levels and improve the duration of, and eligibility for,

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[12] Richard Rubin, "Donald Trump's Tax Ideas Could Boost Debt-Laden Real Estate Firms," *Wall Street Journal*, updated August 18, 2016, https://www.wsj.com/articles/donald-trumps-tax-ideas-could-boost-debt-laden-real-estate-firms-1471542621.

[13] Jim Tankersley, "Trump Eyes New Tax Cuts for New Stimulus Package," *New York Times*, May 5, 2020, https://www.nytimes.com/2020/05/05/business/economy/trump-tax-cuts-coronavirus-stimulus.html.

[14] For businesses earning more than $25 million annually, the 2017 tax law limited the amount of interest payments a business can deduct to 30 percent of the business's adjusted taxable income. The CARES Act somewhat loosened this restriction for 2019 and 2020, making it easier for businesses to deduct their interest payments.

[15] Center on Budget and Policy Priorities, "Policy Basics: Fiscal Stimulus," May 21, 2020, https://www.cbpp.org/research/economy/policy-basics-fiscal-stimulus.

[16] Elizabeth McNichol, Michael Leachman, and Joshuah Marshall, "States Need Significantly More Fiscal Relief to Slow the Emerging Deep Recession," Center on Budget and Policy Priorities, April 14, 2020, https://www.cbpp.org/research/state-budget-and-tax/states-need-significantly-more-fiscal-relief-to-slow-the-emerging-deep.

[17] Dottie Rosenbaum, Stacy Dean, and Zoë Neuberger, "The Case for Boosting SNAP Benefits in Next Major Economic Response Package," Center on Budget and Policy Priorities, April 22, 2020,

unemployment benefits; and enact measures to maintain and bolster health coverage and care, especially through Medicaid. Such measures, which should be designed to remain in place until unemployment is no longer significantly elevated and the economy has significantly recovered, would both provide effective economic stimulus and ease hardship.[18]

https://www.cbpp.org/research/food-assistance/the-case-for-boosting-snap-benefits-in-next-major-economic-response-package.

[18] Chad Stone and Sharon Parrott, "Labor Market Conditions Should Determine Duration, Size of COVID-19 Relief Measures," Center on Budget and Policy Priorities, April 13, 2020, https://www.cbpp.org/research/economy/labor-market-conditions-should-determine-duration-size-of-covid-19-relief-measures.