



The Daily Dish

The Coming Tax Debate

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One of the key fiscal decisions in the next few years will be the fate of the 2017 Tax Cuts and Jobs Act (TCJA) as the vast majority of its provisions sunset at the end of 2025. Recently, the Committee for a Responsible Federal Budget (CRFB) held an event entitled [“When the TCJA Expires: A Tax Policy Summit.”](#) The event featured five plans to follow the TCJA: two “Democratic plans,” two “Republican plans,” and a “centrist plan” by CRFB itself.

Broadly, the TCJA had three key focuses: (a) taxation of C corporations, including multinationals, (b) taxation of pass-through businesses, and (c) individual income taxation. Eakinomics has lots of thoughts on all three, but for the moment, let us focus on the taxation of corporations. The centerpiece of corporate taxation in the 2017 law was cutting the corporate tax rate from 35 percent to 21 percent. On the international front, it moved the United States from taxing the worldwide income of corporations to a territorial system that taxes domestic earnings. This was augmented by a minimum tax on global intangible lightly taxed income (GILTI) and a “patent box” called foreign-derived intangible income (FDII) to keep easily mobile intellectual capital (and thus the income flowing from it) taxed in the United States. Collectively, these provisions addressed the pre-2017 incentives to move headquarters outside the country to escape the combination of a high rate and global reach, to invest outside the United States, and to invest too little overall.

With regard to business income in general, the TCJA permitted the full expensing – i.e., immediate deduction of 100 percent of the cost – for a large fraction of investment and research and development, and limited the deductibility of interest costs. Expensing has the virtue that all kinds of investments – equipment, software, intellectual capital, human capital – would receive exactly the same tax treatment and eliminate tax-based distortions in firms’ activities. Eliminating interest deductibility would do the same for the choice between debt and equity finance; limiting the deductibility lowered the distortion somewhat.

In short, the TCJA did an enormous amount to remove tax-base distortions to location,

investment, and finance decisions in the corporate sector.

It worked spectacularly. In the decade prior to the passage of the TCJA, roughly 10 U.S.-headquartered firms moved their headquarters to an overseas location annually. (Few realize that the New York Stock Exchange – the iconic symbol of American capitalism – is headquartered in the Netherlands for tax purposes.) Since passage, not a single headquarters has been lost. In the most careful study of investment decisions, “[Tax Policy and Investment in a Global Economy](#),” the authors conclude that the TCJA raised investment by 20 percent and that investments abroad stimulated domestic investment as well.

Given this, what do the various tax plans propose? Both Democratic plans had a 28 percent corporate tax rate, while the Republican plans kept the 21 percent rate, and the centrist plan raised it to 25 percent. All the plans made permanent the expensing of R&D (which has lapsed), and all but one plan (Democratic) made investment expensing permanent. This suggests a path forward that makes sense. Make permanent all the expensing provisions and keep the corporate rate at 21 percent. If circumstances dictate that more revenue is needed, additional base broadening such as limiting interest deductibility would do the trick and enhance the efficiency of the tax code.