

**ANALYSIS OF LONG-TERM REVENUE IMPACTS  
OF THE  
PRESIDENT'S TAX REFORM PLAN**

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## INTRODUCTION

One major goal of the President's tax plan is revenue neutrality, which means that the plan is intended to raise about the same revenues as projected under current law from 1986 through 1990. The estimates supplied by the Department of the Treasury show that the President's plan would be approximately revenue neutral over that five-year time span. The Treasury estimates that the difference in overall revenues between the proposal and current law would be \$11.5 billion over the 1986 to 1990 period. This difference in revenues from the entire proposal (less than 0.5 percent of total revenue over the five-year period) is clearly insignificant from an estimating standpoint.

The Treasury Department revenue estimates show that the taxes paid by corporations would increase and those paid by individuals would decrease. In 1990, the Treasury estimates that corporate income taxes would rise by \$25.2 billion (22.7 percent), and individual income taxes would decline by \$26.9 billion (5.2 percent). Over the five-year period from 1986 through 1990, corporate revenues are estimated to rise by \$118.4 billion (24.4 percent), while individual revenues would fall by \$131.8 billion (6 percent).<sup>1</sup> Because of this apparent shift in taxation from individuals to corporations, apprehension has arisen that the new tax system would hurt capital formation and reduce the growth in the economy.

### Revenue Estimates and Revenue Neutrality

The type of revenue estimates used in discussions of tax reform and revenue neutrality are static five-year cash-flow revenue projections. Although these revenue projections are an important part of the budgetary process, they do not account for the full effects of many tax changes. Two important limitations to cash-flow revenue estimates are that they are restricted in their time horizon and that they do not reflect changes in future tax deferrals over time. Because the long-run revenue potential of any new tax system can differ significantly from its short-run revenue effect, limiting the estimation period to five years may provide a misleading indication of a new system's revenue potential and its allocation of tax payments between corporations and individuals. This is especially true if provisions are phased in (or due to expire) during the first five years.

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<sup>1</sup> The Treasury Department also asserts that "when fully effective, the President's proposals would raise total corporate tax payments by an estimated 9 percent, and would lower total individual tax payments by 7 percent." The term "fully effective" is not defined. This would appear to be inconsistent with long-run neutrality because individual receipts under current law are almost five times greater than corporate receipts. See The President's Tax Proposals to the Congress for Fairness, Growth, and Simplicity.



A second limitation of the five-year cash-flow estimates is that they ignore the effect of changes in tax deferrals beyond the five-year period. A tax deferral is a future tax liability that results from current actions. For example, depositing \$2,000 in an Individual Retirement Account (IRA) results in a tax deduction this year and a concomitant future tax obligation (deferral) when those funds are withdrawn. Where tax provisions affect tax liabilities in the future, it is important to look not only at current tax effects, but at those future tax changes as well. In the case of tax deferrals, the present value of a tax change provides useful information about the long-run tax burden that it is likely to impose. The present-value effect also indicates the change that is likely to occur in investment incentives. In order to measure the present value of a tax change, it is often necessary to extend one's time horizon well beyond the conventional five-year time span.

In this study, the Congressional Budget Office (CBO) analyzes the revenue effects of several major corporate income tax provisions included in the President's tax plan. Provisions analyzed here include (among others) the proposed changes in the system of tax depreciation, the investment tax credit (ITC), and the maximum corporate tax rate. These provisions have large revenue effects in 1990; the Treasury estimates that the change in depreciation will raise \$21.2 billion in 1990, repealing the investment tax credit will raise \$44.6 billion, and corporate rate reduction will reduce revenues by \$42.0 billion in that year.<sup>2</sup> The addition of a 10 percent dividends-paid deduction is estimated to lower revenues by \$6.7 billion in 1990.

With the notable exception of the change in depreciation rules, the revenue estimates for these provisions probably provide a fairly accurate account of their longer-run revenue effects relative to GNP since they are immediately phased in and do not give rise to future tax deferrals. The depreciation rule changes, however, do have significant effects on revenues well after 1990 and affect the long-run revenue potential of the proposed tax system. Therefore, the short-run revenue effects associated with the depreciation changes may provide a misleading indication of the future revenues and investment incentives to be generated from such changes. These future revenue effects are the focus of this paper.

#### Other Revenue Provisions

Other provisions of the President's tax plan have major effects on federal revenues. Among these are the rate cuts for individuals (-\$72.7 billion in 1990; -\$260.6 billion in 1986-1990), the change in the personal exemption (-\$48.0 billion in 1990; -\$193.1 billion in 1986-1990), the repeal of the

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<sup>2</sup> The President's Tax Proposals to The Congress for Fairness, Simplicity, and Growth, Appendix C. The rate reduction revenue estimates are calculated assuming enactment of many other base-broadening provisions, in addition to the ones considered here.



deduction for state and local taxes (+\$40.0 billion in 1990; +\$148.9 billion in 1986-1990), the repeal of income averaging (+\$4.9 billion in 1990; +\$8.7 billion in 1986-1990), and the repeal of the second earner deduction (+\$9.0 billion in 1990; +\$33.7 billion in 1986-1990). The President's proposal also includes a recapture of the rate reduction on accelerated depreciation that is estimated to raise \$57.6 billion over the 1986-1989 period, but would have no long-run revenue effect. In general, these provisions result in straightforward tax changes and do not involve long phase-in periods or changes in future taxes; their long-run revenue effects (relative to GNP) are likely to be approximated by their 1990 effects.

There are, however, several other major provisions for which the five year and 1990 revenue estimates may be misleading as to their longer-term revenue effect. These include the matching of income and expense for multi-period production (+\$14.1 billion in 1990; +\$44.0 billion in 1986-1990), the changes in the rules regarding the taxation of capital gains (+\$5.4 billion in 1990; +\$18.5 billion in 1986-1990), the elimination of private-purpose bonds (+\$4.5 billion in 1990; +\$13.0 billion in 1986-1990), taxation of some health insurance benefits (+\$4.0 billion in 1990; +\$17.4 billion in 1986-1990), and tax changes regarding retirement saving (+\$5.8 in 1990; +\$20.6 billion in 1986-1990). The 1990 revenue estimates for these provisions may be significantly different from their long-term revenue effects, relative to GNP. The potential long-run revenue effects from these and other major tax provisions are further discussed in the last section of this paper.

#### Supplemental Estimates of Corporate Tax Provisions

Two sets of supplementary revenue estimates are presented in this paper. The first set looks at the 20-year effects of corporate tax provisions on the taxation of income from a fixed composite corporate investment undertaken today. The second set of estimates extends the time horizon from 5 to 15 years and examines the profile of the cash-flow revenue estimates of the general corporate tax provisions. This second set of estimates is based on aggregate gross corporate investment and includes the effect of the growing level of corporate investment over time.

The basic results of this study indicate that the general corporate provisions included in the President's tax plan (depreciation rule changes, the investment tax credit, the corporate rate cut, and the partial dividend deduction) will probably reduce the tax burden on income earned in the corporate sector in the long run. Compared with current law, this means that the overall effect of these general provisions related to taxing corporations probably provide a tax cut over time. The President's tax proposal may still raise taxes paid by the corporate sector (compared with current law) in the long run because there are many base broadening provisions that affect selected industries, such as oil and gas production, defense contracting, or financial services. However, the longer-run revenue potential of the system as a share of GNP is likely to be much less



than would be shown by a simple extrapolation of five-year revenue estimates to future years.

#### ACCOUNTING FOR TAX DEFERRALS

In those instances where a tax code change results in contingent future tax changes, and these contingent liabilities are ignored, cash-flow revenue estimates may not accurately reflect the long-run revenue effect of the change. In these cases, revenue estimates based on the concept of present value may be a better measure of the full revenue cost to the Treasury because they account for all current and future tax deductions and payments. (Present value revenue estimates could be a useful supplement to the traditional five-year revenue estimates that are required as part of the annual federal government budget process.)

#### Depreciation and Timing

Because depreciation by its nature deals with the timing of deductions for capitalized expenditures, the evaluation of the full stream of deductions--not just the first five years--is necessary to measure the relative generosity of alternative depreciation systems. In addition, because depreciation rules affect most businesses and the President's plan calls for a basic overhaul of the current system of depreciation, a proper evaluation of the long-run effects of these changes is of utmost importance.

Consider, for example, a firm that decides to invest in a machine that makes steel belted radial tires. The machine produces 100 tires per year for 10 years and then is retired. The machine earns a profit of \$30 per tire in the first year. Because of increased operating costs and more intense competition from newer and more efficient machines, however, the profit per tire goes down by 10 percent each year. For simplicity, it is assumed that there is no price inflation. The machine is placed in service midway through the first tax year. Table 1 displays the output and revenue stream for the machine over time.

Under current law, the machine is considered five-year property under the Accelerated Cost Recovery System (ACRS). The deductions for depreciation are shown in the fourth column of the table; the tax payments under ACRS are shown in the fifth column.<sup>3</sup> The depreciable basis for the machine

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<sup>3</sup> Under current law, the machine would also be eligible for the investment tax credit along with its requirement for a 50 percent basis adjustment. In this example used here, only the effect of the depreciation schedule is shown--the investment credit and basis adjustment are not taken into account. In the full simulations presented below, both these provisions are included.



TABLE 1. CALCULATION OF TAXES UNDER ACRS AND ECONOMIC DEPRECIATION (In dollars)

Year	Output (tires per year) (1)	Net Revenue Per Tire (2)	Annual Net Revenue (3)	Depre- ciation Under ACRS (4)	Tax <sup>a</sup> (5)	Economic Depre- ciation <sup>b</sup> (6)	Tax (7)	Tax Change (8)	Cumulative Tax Change (9)
1	50	30	1,500	1,968	-215	582	422	637	637
2	100	27	2,700	2,886	-85	1,823	404	489	1,127
3	100	24	2,430	2,755	-149	1,680	345	494	1,621
4	100	22	2,187	2,755	-261	1,555	291	552	2,173
5	100	20	1,968	2,755	-362	1,445	241	603	2,775
6	100	18	1,771	0	815	1,349	194	-621	2,155
7	100	16	1,594	0	733	1,266	151	-583	1,572
8	100	14	1,435	0	660	1,196	110	-550	1,022
9	100	13	1,291	0	594	1,136	72	-522	500
10	100	12	1,162	0	535	1,086	35	-500	0
Sum:			18,040	13,117	2,264	13,117	2,264	0	
Present Value: <sup>c</sup>					1,436		1,916	479	
Effective Tax Rate:					34%		46%		

SOURCE: Congressional Budget Office.

- a. Does not take into account the investment tax credit allowed under current law.
- b. Economic depreciation is defined as the change in the market value of the machine over time. The market value of the machine at any point in time is the present value of its remaining net revenue stream.
- c. Discounted at the after-tax return of 4.6 percent calculated under ACRS.



is \$13,117 and is the machine's original acquisition cost. This cost is derived by assuming it equals the present value of the machine's expected revenue stream over its entire life. The revenue stream (column three) is discounted at 7 percent to arrive at the machine's acquisition cost.

The tax payments under ACRS are negative in the first five years. This reflects the fact that the ACRS schedule is accelerated and allows companies to earn deductions in excess of economic income in the first few years of the asset's life. (The investment credit is ignored in this example.) Starting in the sixth year, the firm starts paying tax on the income from the machine since ACRS deductions have been exhausted. In effect, the company pays higher taxes in these years to "pay off" the tax saving it accrued over the first five years. In this example, the tax reduces the after-tax rate of return to 4.6 percent. The present value of tax payments (discounted at 4.6 percent) is \$1,436 and the effective tax rate on the asset is 34 percent.<sup>4</sup>

Now, suppose the tax law is changed to allow only economic depreciation for tax purposes.<sup>5</sup> The deductions under economic depreciation are shown in column six of the table; the new stream of tax payments under economic depreciation is shown in column seven. The new present value of tax payments is \$1,916 and the effective tax rate on the asset is the statutory rate of 46 percent.

Under the new depreciation policy, the sum of tax payments has not changed, equaling \$2,264 in each case. The present value of the taxes under economic depreciation is \$479 greater than under ACRS because the timing of the payments has been shifted forward. Because a dollar is worth more now than in the future, the change to the less accelerated depreciation system raises the present value of future tax payments.

In a year-by-year comparison, the change would result in a tax increase in each of the first five years and a tax decrease in each of the next five years. In the first year, the depreciation change would result in a tax increase of \$637. By the fifth year, the cumulative tax increase would be \$2,775--the amount that revenue estimators would record as the five-year change in taxes for this particular asset. In the tire machine example, the five-year estimate takes no account of the fact that an equivalent tax decrease will occur in the subsequent five years. The result: a five-year estimate (\$2,775) that records a tax increase almost six times larger than the present value amount (\$479). In other words, the five-year cumulative

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<sup>4</sup> The effective tax rate is the difference between the pretax rate of return and the after-tax rate of return divided by the pretax rate of return.

<sup>5</sup> Economic depreciation provides an interesting illustrative case because it delays depreciation deductions, compared to current law, but keeps the total amount unchanged. Therefore, tax payments on the return to any single investment are not changed in their amount, but only in their timing.



revenue effect exceeds the present value revenue increase by a factor of about six.

Five-year cash-flow estimates may provide an incomplete view of the financial implications of the tax changes that involve future revenue effects. Unlike tax provisions that do not give rise to tax deferrals, the five-year cash-flow tax increases due to a deceleration of depreciation deductions are associated with tax reductions in future years. On a per dollar basis, current tax increases that do not involve future tax reductions are worth much more to the Treasury in terms of increased revenues than is a change that simply alters the time pattern of tax payments, but not their total amount.<sup>6</sup>

The implication of this result is quite significant in the debate over tax reform and revenue neutrality. For example, suppose a tax system is enacted that institutes economic depreciation. The five-year cumulative tax increase on income from the tire-making machine would be \$2,775 when compared with ACRS. Also suppose that, in the spirit of revenue neutrality, this amount is used to increase personal exemptions or some other revenue-reducing option resulting in an equal tax loss. For the first five years, the system would remain revenue neutral; after that a sizable loss of revenue would occur (measured relative to current law). Over the next five years, cumulative revenue losses of \$2,775 would be accrued and the new tax system would turn from revenue neutral to a revenue loser relative to current law. On a present value basis, the tax increase over the life of the machine would actually be \$479--the present value of tax reductions that can be financed by the depreciation change. The implication of this result is that the move from a front-loaded depreciation system to economic depreciation, considered alone, can appear to raise taxes significantly on corporations in the near future when the tax increase may be only moderate, or even a tax decrease, in present value terms over a longer time frame.

Clearly, in the transition from ACRS (with its front-loaded depreciation deductions) to economic depreciation (where deductions are spread out over a longer period), some firms will experience a sharp increase in tax payments during the first few years. The large immediate tax increase could impose a sizable burden on corporate cash flow. Offsetting this, however, would be future tax reductions. Theoretically, companies should be able to borrow against these reductions, thereby evening out their cash flow.<sup>7</sup>

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<sup>6</sup> For example, a current tax increase from repealing the investment tax credit is likely to be worth much more than a current tax increase resulting from changing the timing of depreciation deductions.

<sup>7</sup> This assumes, of course, that financial markets recognize future tax reductions as an asset of the corporation. To the extent that financial institutions view any long-term receivable as an asset, future depreciation deductions may be regarded the same way. On the other hand, firms (and their lenders) may be uncertain about the realization of future tax deductions and discount their value quite heavily. If so, companies



## The President's Plan

The President's tax reform proposal includes several basic changes in the taxation of corporate income. The proposal repeals the investment tax credit, institutes a new system of depreciation and lowers the top corporate tax rate from 46 percent to 33 percent.<sup>8</sup> The new depreciation system stretches out depreciation compared with ACRS and indexes the system for inflation. The combination of the depreciation changes and elimination of the ITC reduces differences in effective tax rates among assets. As the above discussion points out, this type of tax change is likely to produce a tax increase relative to current law within the first few years of enactment for depreciable assets purchased after the tax change, and a tax decrease relative to current law in later years. When aggregated across all assets purchased in a given year, the same effects will occur. Therefore, sole reliance on five-year revenue estimates (calculated on the traditional cash-flow basis) will provide a misleading indication of the change in taxes paid on the income earned by a given asset purchased after the tax change.<sup>9</sup>

The tax payments attributable to a single hypothetical corporate investment under the alternative tax depreciation systems has been calculated to compare five-year revenue estimates and present value revenue estimates of changes in tax policy.<sup>10</sup> The hypothetical investment is a \$10,000 permanent increase in the real stock of capital goods that roughly mirrors the current composition of the U.S. corporate capital stock. Therefore, the tax payments and tax rates calculated here are intended to reflect those related to this marginal increase in the capital stock.

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may expect to have sizable short-run difficulties.

<sup>8</sup> The proposal also calls for a 10 percent dividends-paid deduction and a recapture of the rate reduction for accelerated depreciation.

<sup>9</sup> Unlike the depreciation change, the rate reduction and repeal of the ITC do not give rise to major tax effects in the future. (The repeal of the ITC will have some small out-year effects to the extent that the current 50 percent basis adjustment reduces future depreciation deductions. Repealing it would therefore increase depreciation deductions in the future. Repealing the ITC may also have future tax effects to the extent that credits that are presently carried over would be utilized sooner rather than later.) Therefore, the cash-flow estimates of the revenue effects of these changes are likely to be much more indicative of their actual longer-term effect on corporate tax burdens.

<sup>10</sup> The changes considered here are the rate cut, the new depreciation system and the repeal of the investment tax credit. The dividends-paid deduction and the recapture of the rate reduction on accelerated depreciation are not considered in the analysis of the composite investment.



The simulated investment consists of buildings, equipment and machinery, and inventories. The initial investment shares are shown in Table 2. It is assumed that once the investment has been made, subsequent investment (equal to the economic depreciation of the new capital stock) is undertaken in order to maintain the real value of the new capital over time. (Because this is a static analysis of the tax proposal, it is assumed that the composition of the capital stock does not change in response to the changes in tax rules.)

Changes in depreciation apply not only to increases in the capital stock, but to replacement investment as well. Therefore, in actually calculating five-year revenue estimates (such as those in the second part of this paper), both replacement and net new investment (the sum of which is gross investment) must be taken into account. Because the composition of the capital stock is weighted more heavily toward long-lived assets, such as buildings and structures, rather than short-lived assets, such as equipment and machinery, the revenue profile associated with this simulated investment will not be directly comparable with those based on gross investment flows that are presented in the second part of this paper.<sup>11</sup>

In the simulation, the investment is assumed to be made at the start of the year; income and tax deductions start to be realized at the end of six months, and occur every six months thereafter. The firm is assumed to require a 4 percent real after-tax return and is subject to the 46 percent top statutory tax rate. The inflation rate is assumed to remain a constant 4 percent. The firm is assumed to maintain the real size of its new capital stock by reinvesting an amount sufficient to offset any real economic depreciation (that is, the investment remains at \$10,000 in real terms in perpetuity). The model is solved by determining the annual gross revenue the firm must earn in order to yield its 4 percent required return. The investment is assumed to be financed out of retained earnings.

The model takes into account the different ACRS depreciation rates that apply to each of the different types of assets in the capital stock. The investment tax credit (ITC) under current law, with the 50 percent basis adjustment, is also included in the model.

Table 3 compares tax payments for this representative investment under current law and the President's plan. The first two columns show the tax payments under current law and those that would be payable under the President's plan (at the 33 percent tax rate). The tax increase in the first year of such a change would be \$551. The first year increase is largely attributable to the repeal of the investment tax credit. Over the first five years, the cumulative tax increase is \$886 which has a present value of \$757. In the sixth year and thereafter, however, the new system loses revenue each year relative to current law. By the end of 20 years,

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<sup>11</sup> The time profile of the revenue estimates will also differ because the simulated investment remains constant in real terms, whereas the revenue estimates in the second part of this study account for continuing growth in the capital stock.



**TABLE 2. COMPOSITION OF CAPITAL GOODS IN SIMULATED INVESTMENT**

Asset Type	Percentage of Investment
Industrial Buildings	9.6
Commercial Buildings	9.3
Railroad Structures	2.7
Telephone and Telegraph Facilities	4.0
Electric Light and Power Facilities	9.8
Gas Facilities	2.6
Petroleum Pipelines	0.9
Furniture and Fixtures	1.8
Fabricated Metal Products	1.7
Engines and Turbines	1.0
Tractors	0.9
Agricultural Machinery	2.1
Construction Machinery	1.1
Mining and Oilfield Machinery	0.9
Metalworking Machinery	2.5
Special Industry Machinery	2.6
General Industrial Machinery	2.4
Office, Computing, and Accounting Machinery	2.1
Service Industry Machinery	0.9
Electrical Transmission, Distribution, and Communications Equipment	6.5
Trucks, Buses, and Trailers	2.2
Automobiles	1.1
Aircraft	0.8
Ships and Boats	0.8
Railroad Equipment	1.7
Instruments	2.3
Other Equipment	1.0
Inventories	25.0
<b>Total</b>	<b>100.0</b>

**SOURCE:** Congressional Budget Office estimates based on National Income and Products Accounts investment data.



**TABLE 3. CORPORATE TAX PAYMENTS FOR PERMANENT \$10,000 INCREASE IN CAPITAL STOCK UNDER CURRENT LAW AND THE PRESIDENT'S PLAN**

Year	Taxes Under:		Increase or Decrease	Cumulative Change
	Current Law	President's Plan		
1	-573	-22	551	551
2	-51	-32	19	570
3	-59	17	77	647
4	-73	39	112	759
5	-91	36	127	886
6	205	23	-182	704
7	222	42	-181	524
8	242	146	-96	428
9	252	148	-104	324
10	263	152	-111	213
11	278	239	-39	173
12	290	247	-43	130
13	313	256	-57	74
14	326	265	-61	13
15	340	275	-65	-52
16	400	284	-116	-168
17	416	294	-122	-290
18	433	305	-129	-418
19	471	316	-155	-574
20	510	327	-183	-757
Present Value (5 years)	-738	19	757	
Present Value (20 years)	1,024	1,135	111	
Present Value (In perpetuity)	3,853	3,077	-775	

**SOURCE:** Congressional Budget Office.



the cumulative revenue loss is \$757. The present value of the taxes paid increases by \$111 over the first 20 years, but declines by \$775 when calculated over an infinite number of years.

The effective tax rate calculated in this model on the overall investment under current law is about 29 percent. This tax rate is higher than effective corporate tax rates reported elsewhere, primarily because it accounts for the 25 percent of the corporate capital stock that consists of highly-taxed inventories.<sup>12</sup> LIFO accounting is assumed to be used for inventories, therefore resulting in an effective tax rate equal to the statutory tax rate. The effective tax rate is equal to the statutory tax rate on LIFO inventories because the real return--and only the real return--is taxed in full.

The effective tax rate on corporate capital is reduced by the new policy, in spite of the apparent tax increase indicated by the five-year revenue effect. The effective corporate tax rate on this equity-financed investment is calculated at 24 percent--well below the 29 percent effective corporate tax rate calculated under current law. (The Treasury estimates that the effective corporate tax rate from the President's plan will be reduced from 35 percent under current law to 25 percent under the reform proposal.<sup>13</sup>) Both sets of effective tax rate estimates are for the corporate level tax only and are based on an investment fully financed by equity. They do not take into account any proposed changes in personal income taxation that affect income from corporate capital, nor do they account for debt finance.<sup>14</sup> As has been noted elsewhere, when these factors are included, the overall effective tax rate on income earned in

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<sup>12</sup> For example, Alan J. Auerbach, in "Corporate Taxation in the United States," Brooking Papers on Economic Activity 2:1983, (Washington, D.C.: Brookings Institution, 1984) pp. 451-513, does not include inventories in his computation of the overall effective corporate tax rate.

<sup>13</sup> The President's Tax Proposals to the Congress for Fairness, Growth, and Simplicity, p. 159. The differences in effective tax rates (between the Treasury estimates and CBO estimates) are primarily due to differences in the estimated asset composition of the corporate capital stock.

<sup>14</sup> Changes (not included here) that affect the overall taxation of income earned in the corporate sector include the reduction in individual tax rates, the decrease in the exclusion for capital gains, and the dividends-paid deduction. Debt finance may affect the overall taxation of corporate source income because interest payments are deductible to corporations and are taxable to lenders, who may be in a different tax bracket.



the corporate sector may actually increase under the President's proposal.<sup>15</sup>

This analysis suggests that the general corporate tax provisions included in the President's tax plan might result in lower corporate revenues (compared to current law) when measured in present value terms over an extended time horizon. Other specific corporate provisions, however, may still serve to increase the overall revenues raised by the corporate tax in the long-run. Moreover, the time pattern of the actual revenue changes in the first 20 years will differ from that shown in Table 3 because of growth in the level of investment. The next section presents CBO's estimates of the revenue effects of the major corporate tax provisions for the next 15 years, based on CBO assumptions about the future growth pattern of investment.

#### REVENUE EFFECTS OF MAJOR CORPORATE TAX PROVISIONS

The following sections provide a preliminary CBO estimate of the pattern of revenue effects for the general corporate provisions of the Administration's recent tax reform proposal over the first 15 years, a decomposition of the first five years of this estimate into the four general provisions (with the revenue effects of the rest of the corporate provisions in the proposal combined with the effect of the rate reduction), and a comparison of the components with the Treasury's revenue estimates for the proposal. The methodology and economic assumptions used to produce CBO's estimates are described in the Appendix. For the first five years these estimates, which are sensitive to economic assumptions, are based on CBO's baseline economic projections of February 1985, that assume less real growth and more inflation than the Administration's estimates. These estimates are not intended to be substitutes for official revenue estimates provided by the Joint Committee on Taxation. The JCT is currently refining its methodology, and plans to release estimates of the revenue effects of the President's proposal.

#### Additional Depreciation Deductions Resulting From CCRS

Table 4 shows the change from current law in the corporate depreciation deductions that would result from the capital cost recovery system (CCRS) proposed by the Administration. CCRS would increase depreciation deductions, relative to current law, in each of the next 15 years except 1989 and 1990. The two years in which CCRS would reduce depreciation deductions relative to current law are 1989 and 1990, the years in which deductions for investment put in place after 1985 would peak under the accelerated cost recovery system (ACRS) of current law.

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<sup>15</sup> See Don Fullerton, Testimony Before the Senate Finance Committee, June 20, 1985.



**TABLE 4. CHANGES IN AGGREGATE CORPORATE DEPRECIATION DEDUCTIONS DUE TO CCRS (CCRS MINUS ACRS)**

<b>Calendar Year</b>	<b>Billions of Dollars</b>	<b>Percent of GNP</b>
1986	4.0	0.1
1987	17.7	0.4
1988	6.5	0.1
1989	-5.6	-0.1
1990	-22.0	-0.4
1991	4.1	0.1
1992	25.3	0.4
1993	39.2	0.6
1994	45.2	0.6
1995	51.7	0.6
1996	54.2	0.6
1997	55.2	0.6
1998	55.9	0.6
1999	56.7	0.5
2000	57.8	0.5

**SOURCE: Congressional Budget Office.**