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Adding Bonus Expensing to the Camp Tax Reform Plan

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Introduction

Congress is currently considering tax extenders, the renewal of expiring or recently expired tax provisions. Among the provisions is 50 percent bonus expensing, otherwise known as bonus depreciation. The extender provision passed by the House Ways and Means Committee, currently under consideration by the whole House of Representatives, would make 50 percent bonus expensing a permanent feature of the U.S. cost recovery system.

Fifty percent bonus expensing allows businesses to immediately write off, or expense, half of their investment in equipment and short-lived structures (assets with twenty year lives or less). It does not apply to commercial and residential buildings or factories.

Bonus expensing moves the timing of depreciation write-offs closer to the time of purchase. This brings the write-offs closer to the full value of the cost of the investment, reducing the after-tax cost of acquiring capital assets and moving the tax treatment of cost recovery toward tax neutrality (when taxes fall with equal impact on income used for investment or consumption).

If made permanent, bonus expensing would induce firms to acquire and maintain a larger stock of equipment. The added capital would expand domestic production, raise productivity and wages, and increase employment.

Adding Bonus Expensing to the Camp Plan Would Grow the Economy, Lift Wages, and Raise Revenue

In previous papers,[1] we used the Tax Foundation's Taxes and Growth Model to examine the effect of the tax reform proposal recently released by Ways and Means Chairman Dave Camp (R-MI), and, separately, to model the effect of adding 50 percent bonus expensing to present law. In this paper, we model the effect of adding 50 percent bonus expensing to the Camp proposal.

1 *See, e.g.*, Stephen J. Entin, Michael Schuyler, & William McBride, An Economic Analysis of the Camp Tax Reform Discussion Draft, Tax Foundation Special Report No. 219 (May 14, 2014), http://taxfoundation.org/article/economic-analysis-camp-tax-reform-discussion-draft. *See also* William McBride, Some Tax Cuts Pay for Themselves, Tax Foundation Tax Policy Blog, May 29, 2014, http://taxfoundation.org/blog/some-tax-cuts-pay-themselves.

Our original estimate of the Camp proposal (see Table 1, column 1) projected an ultimate increase in the level of GDP of 0.2 percent after all economic adjustments (a gain in annual output in the long term of about $35.5 billion in 2013 dollars). Adding permanent 50 percent bonus expensing to the Camp plan (see Table 1, column 2) increases the projected economic gain to about 1.8 percent of GDP (about $295.3 billion dollars of additional yearly output). That is measured against current law, in which the previous bonus expensing has been allowed to lapse.

We estimate that the Camp plan with bonus expensing would raise annual federal revenue from all sources on a dynamic basis (*i.e.*, after accounting for economic growth) by $12.4 billion compared to the current law baseline. The additional growth-related revenue would fully offset the projected static revenue loss of $52.8 billion estimated by ignoring the economic gains.

With bonus expensing attached to the Camp tax reform plan, hours worked would rise by about 0.8 percent, equivalent to 780,500 full time equivalent jobs. This is nearly 300,000 more jobs than without the provision. The capital stock would increase by about 4.4 percent; it would decline slightly without the bonus expensing provision. The wage rate would rise by over 1.1 percent with the bonus expensing compared to a small decline without it.

Table 1. Positive Effects of Adding Bonus Expensing to the Camp Tax Reform Plan

Economic and Budget Changes vs. Current Law
(Billions of 2013 dollars except as noted)

	Camp Draft vs. Current Law	Camp Draft Adding 50% Bonus Expensing
GDP	0.22%	1.81%
$GDP ($ billions)	$35.5	$295.3
Private business GDP	0.27%	1.93%
Private business stocks	-0.18%	4.41%
Wage rate	-0.21%	1.13%
Private business hours of work	0.50%	0.81%
Jobs (thousands)	486	780.5
Static federal revenue estimate, GDP assumed constant ($ billions)	-$30.4	-$52.8
Dynamic federal revenue estimate after GDP gain or loss ($ billions)	-$21.2	$12.4
Weighted average service price	% Change	% Change
Corporate	0.48%	-2.84%
Noncorporate	0.46%	-1.23%
All business	0.47%	-2.36%

Conclusion

The addition of permanent bonus expensing would improve the economic effects of Chairman Camp's tax reform proposal, increasing the resulting economic growth to over 1.8 percent (up from 0.2 percent), adding 780,500 jobs (up from 486,000), and increasing wages by over 1.1 percent (up from -0.21 percent).

Bonus expensing would produce significant gains in capital formation, wages, and employment. These gains in national income would result in higher tax revenues for federal, state, and local governments. The adoption of permanent bonus expensing is a costless way of improving economic performance and raising living standards.

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