Congressional Research Service
Informing the legislative debate since 1914

Business Tax Provisions Expiring in 2020, 2021, and 2022 ("Tax Extenders")

Molly F. Sherlock, Coordinator
Specialist in Public Finance

Jane G. Gravelle
Senior Specialist in Economic Policy

Sean Lowry
Analyst in Public Finance

Donald J. Marples
Specialist in Public Finance

March 13, 2020

Congressional Research Service
7-....
www.crs.gov
R46271

CRS REPORT
Prepared for Members and
Committees of Congress

Congressional Research Service
Informing the legislative debate since 1914

Business Tax Provisions Expiring in 2020, 2021, and 2022 ("Tax Extenders")

R46271

March 13, 2020

Molly F. Sherlock, Coordinator
Specialist in Public Finance
-redacted-@crs.loc.gov

Jane G. Gravelle
Senior Specialist in Economic Policy
-redacted-@crs.loc.gov

Sean Lowry
Analyst in Public Finance
-redacted-@crs.loc.gov

Donald J. Marples
Specialist in Public Finance
-redacted-@crs.loc.gov

SUMMARY

Thirteen temporary business tax provisions are scheduled to expire at the end of 2020. Four other temporary business tax provisions are scheduled to expire in 2021 or 2022. In the past, Congress has regularly acted to extend expired or expiring temporary tax provisions. Collectively, these temporary tax provisions are often referred to as "tax extenders."

This report briefly summarizes and discusses the economic impact of the 17 business-related tax provisions that are scheduled to expire in 2020, 2021, or 2022. The provisions discussed in this report are listed below, grouped by type and scheduled year of expiration.

The following special business investment (cost recovery) provisions are scheduled to expire in 2020:

- special expensing rules for certain film, television, and live theatrical productions;
- seven-year recovery period for motorsports entertainment complexes;
- three-year depreciation for race horses two years or younger; and
- accelerated depreciation for business property on an Indian reservation.

The following economic development provisions are scheduled to expire in 2020:

- empowerment zone tax incentives;
- American Samoa economic development credit; and
- new markets tax credit.

The following other business-related provisions are scheduled to expire in 2020:

- Indian employment tax credit;
- mine rescue team training credit;
- employer tax credit for paid family and medical leave;
- work opportunity tax credit;
- look-through treatment of payments between related controlled foreign corporations; and
- provisions modifying excise taxes on wine, beer, and distilled spirits.

The following provisions are scheduled to expire in 2021 or 2022:

- 12.5% increase in low-income housing tax credit (LIHTC) authority;
- computation of adjusted taxable income without regard to any deduction allowable for depreciation, amortization, or depletion;
- the rum cover over; and
- credit for certain expenditures for maintaining railroad tracks.

The 13 temporary business-related tax provisions scheduled to expire at the end of 2020 were most recently extended by the Further Consolidated Appropriations Act of 2020 (P.L. 116-94). Of these 13 provisions, 8 had expired in 2017 and were extended retroactively and 5 were scheduled to expire in 2019. Past tax extenders legislation had extended 11 of these 13 provisions. The other two provisions, both of which were scheduled to expire in 2019, were added to the tax code as part of the 2017 tax revision (P.L. 115-97). Four other business-related provisions will expire in 2021 or 2022.

This report does not include provisions that in the past have been classified as individual or energy-related. See CRS Report R46243, *Individual Tax Provisions ("Tax Extenders") Expiring in 2020: In Brief*, coordinated by Molly F. Sherlock; and CRS Report R44990, *Energy Tax Provisions That Expired in 2017 ("Tax Extenders")*, by Molly F. Sherlock, Donald J. Marples, and Margot L. Crandall-Hollick. For a general overview of tax extenders, see CRS Report R45347, *Tax Provisions That Expired in 2017 ("Tax Extenders")*, by Molly F. Sherlock.

Contents

Tables

Contacts

Introduction

In the past, Congress has regularly acted to extend expired or expiring temporary tax provisions.[1] Collectively, these temporary tax provisions are often referred to as "tax extenders." This report briefly summarizes and discusses the economic impact of the 17 business-related tax provisions that are scheduled to expire before 2025.[2]

There are 13 business-related temporary tax provisions scheduled to expire at the end of 2020. Most of these business-related provisions were included in past extenders legislation. The business tax extenders are diverse in purpose, providing various types of tax relief to businesses in different industries. Most recently, Congress extended expiring provisions in the Taxpayer Certainty and Disaster Tax Relief Act of 2019, enacted as Division Q of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94). This law retroactively extended, through 2020, eight temporary tax provisions that had expired at the end of 2017; it also extended five provisions scheduled to expire in 2019.

The estimated cost of the 13 temporary business tax provision extensions enacted in the Further Consolidated Appropriations Act, 2020 (P.L. 116-94) is provided in **Table 1**. The most costly of these provisions are the employer credit for paid family and medical leave ($2.2 billion), the work opportunity tax credit ($2.0 billion), and the New Markets Tax Credit ($1.5 billion). Note that all three of these provisions were scheduled to expire at the end of 2019, and thus were extended for one year. In contrast, the eight other provisions that had expired at the end of 2017 and were extended through 2020 were effectively extended for three years.

Four other business-related provisions are scheduled to expire in 2021 or 2022: (1) the 12.5% increase in the annual low-income housing tax credit (LIHTC) authority for four years (2018-2021), enacted as part of the 2018 Consolidated Appropriations Act, with a cost of $2.7 billion;[3] (2) the computation of adjusted taxable income without regard to any deduction allowable for depreciation, amortization, or depletion for purposes of the interest deduction limit, set to expire by the 2017 tax revision (the Tax Cuts and Jobs Act, P.L. 115-97), with no separate cost estimate for this feature; (3) the five-year extension of the rum cover over, last extended retroactively for 2017 and forward through 2021 as part of the Bipartisan Budget Act of 2018 (P.L. 115-123), with a cost of $0.6 billion;[4] and (4) the credit for certain expenditures for maintaining railroad tracks, extended through 2022 in the Taxpayer Certainty and Disaster Tax Relief Act of 2019, with a cost of $1.1 billion.[5]

There are several options for Congress to consider regarding temporary provisions. Provisions that are scheduled to expire or have expired could be extended, and the extension could be short

---

[1] For an overview of tax extenders, see CRS Report R45347, *Tax Provisions That Expired in 2017 ("Tax Extenders")*, by Molly F. Sherlock.

[2] Numerous provisions will expire after 2025 under the provisions of the 2017 tax revision, P.L. 115-97, popularly known as the Tax Cuts and Jobs Act; these provisions are not discussed in this report. There are no business-related provisions scheduled to expire in 2023 or 2024.

[3] Joint Committee on Taxation, *Estimated Budget Effect of the Revenue Provisions Contained in the House amendment to the Senate amendment to H.R. 1625*, March 22, 2018, JCX-7-18.

[4] Joint Committee on Taxation, *Estimated Budget Effect of the Revenue Provisions Contained in the "Bipartisan Budget Act of 2018,"* February 8, 2018, JCX-4-18.

[5] Joint Committee on Taxation, *Estimated Budget Effect of the Revenue Provisions Contained in the House Amendment to the Senate Amendment to H.R. 1865, The Further Consolidated Appropriations Act, 2020,* December 17, 2019, JCX-54-19R.

term, long term, or permanent. Alternatively, Congress could allow the provisions to expire and remain expired.

Table 1. Estimated Cost of Extending Expired Business Tax Provisions Through 2020
(billions of dollars)

Provision	Cost of Extension in P.L. 116-94
Special Business Investment (Cost Recovery) Provisions	
Special Expensing Rules for Certain Film, Television, and Live Theatrical Productions	-i-
Seven-Year Recovery Period for Motorsports Entertainment Complexes	$0.2
Three-Year Depreciation for Racehorses Two Years or Younger	-i-
Accelerated Depreciation for Business Property on an Indian Reservation	$0.2
Economic Development Provisions	
Empowerment Zone Tax Incentives	$0.8
American Samoa Economic Development Credit	-i-
New Markets Tax Credit*	$1.5
Other Business Provisions	
Indian Employment Tax Credit	$0.2
Mine Rescue Team Training Credit	-i-
Employer Credit for Paid Family and Medical Leave*	$2.2
Work Opportunity Tax Credit*	$2.0
Look-through Treatment of Payments Between Related Controlled Foreign Corporations*	$0.7
Provisions Modifying the Excise Tax Rates of Wine, Beer, and Distilled Spirits*	$1.0

Sources: Joint Committee on Taxation, *Estimated Budget Effect of the Revenue Provisions Contained in the House Amendment to the Senate Amendment to H.R. 1865, The Further Consolidated Appropriations Act, 2020,* December 17, 2019, JCX-54-19R.

Notes: The cost estimates are estimated reductions in revenue over a 10-year budget period (FY2020-FY2029). An "-i-" indicates an estimated revenue loss of less than $50 million between FY2020 and FY2029. An asterisk indicates the four provisions that were scheduled to expire in 2019. All other provisions had expired in 2017.

Provisions Expiring in 2020

There are 13 business-related provisions scheduled to expire in 2020. All 13 of these provisions were extended in the Taxpayer Certainty and Disaster Tax Relief Act of 2019, enacted as Division Q of the Further Consolidated Appropriations Act, 2020 (P.L. 116-94).

Special Business Investment (Cost Recovery) Provisions

The cost of assets that provide services over a period of time, such as machines or buildings, is deducted over a period of years as depreciation. The schedule of depreciation deductions depends on the asset's life and the distribution of deductions over that life. Straight-line depreciation is used for structures, where equal amounts are deducted in each year. For equipment, deductions are accelerated, with larger amounts deducted in earlier years. Equipment is most commonly depreciated over 5 years or 7 years, but some short-lived assets are depreciated over 3 years and some longer-lived assets are depreciated over 10, 15, or 20 years. Nonresidential structures are depreciated over 39 years. Aside from the desire for economic stimulus, traditional economic theories suggest that tax depreciation should match economic (physical) depreciation of assets as closely as possible.

The depreciation provisions discussed below all allow earlier deductions for depreciation, which are valuable because of the time value of money. A fixed reduction in tax liability today is worth more than that same fixed reduction in tax liability in the future. Expensing provisions allow a firm to deduct the cost of an asset the year it is placed in service.

Through 2022, bonus depreciation of 100% allows for full expensing of investments in qualifying equipment and property.[6] It is scheduled to decrease to 80% in 2023, 60% in 2024, 40% in 2025, 20% in 2026, and 0% for property acquired and placed in service in 2027 and thereafter. The presence of bonus depreciation or expensing would make some temporary provisions more important (such as the benefits for motorsports complexes, which would otherwise become ineligible) and some less important (such as shortening lives for racehorses or Indian reservation property, or expensing for films and television, which would have received the benefit regardless).

Special Expensing Rules for Certain Film, Television, and Live Theatrical Productions[7]

Investments in film and television productions are generally recovered using the income forecast method. Under this method, depreciation deductions are based on the pattern of expected earnings.

The American Jobs Creation Act of 2004 (P.L. 108-357) included special rules to allow expensing for certain film and television production costs. The provision's main purpose was to discourage "runaway" productions, or the production of films and television shows in other countries, where tax and other incentives are often offered. Initially, the provision was set to expire at the end of 2008. However, since 2008, the provision has regularly been extended as part of tax extender legislation—most recently in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).[8]

Under the special expensing rules for film, television, and live theatrical productions, taxpayers may elect to deduct immediately up to $15 million of production costs ($20 million for productions produced in certain low-income and distressed communities) in the tax year incurred. Eligible productions are limited to those in which at least 75% of the compensation paid is for services performed in the United States. For productions that started before 2008, the expensing deduction is not allowed if the aggregate production cost exceeds $15 million ($20 million for productions in designated low-income and distressed communities). Qualifying live theatrical productions are those generally performed in venues with an audience capacity of not more than 3,000 (or 6,500 for seasonal productions performed no more than 10 weeks annually). The

[6] For more information, see CRS Report RL31852, *The Section 179 and Section 168(k) Expensing Allowances: Current Law and Economic Effects*, by Gary Guenther.

[7] Internal Revenue Code (IRC) §181(f).

[8] The bonus depreciation provided in the 2017 tax revision (P.L. 115-97), allowing for 100% bonus depreciation through 2022 and phasing out afterward to 0% after 2026, expands the definition of qualified property for the purposes of claiming bonus depreciation to include the production costs of qualified film, television, and live theatrical productions.

provisions would cover most theatrical productions (the largest of the Broadway theatres, for example, has a seating capacity of less than 2,000).[9]

The ability to expense (deduct immediately) certain film, television, and live theatrical production costs provides a benefit by allowing deductions to be taken earlier, thus deferring tax liability. The magnitude of the benefit depends on the average lag time from production to earning income. For many films, production costs would be deductible in the year the film is released. If the film is released one year after the production costs are incurred, which may be the case for independent and smaller productions, the provision accelerates cost recovery by one year. The benefit conferred by accelerating cost recovery deductions by one year is limited. Taxpayers with limited or no tax liability may derive little or no benefit from the expensing allowance.

The primary policy objective of providing special tax incentives for film and television producers is to deter productions from moving overseas, lured by lower production costs as well as tax and other subsidies offered by foreign governments. Because live theatre is tied to audience location, runaway productions are not a concern. However, providing expensing for live theatrical production costs could encourage investment in such productions and provide parity with film and television. In evaluating this incentive, one consideration is the economic value of domestic film, television, and theatre production relative to the cost of the targeted tax benefits.

Seven-Year Recovery Period for Motorsports Entertainment Complexes[10]

An exception from the 39-year depreciation life for nonresidential structures exists for the theme and amusement park industry. Assets in this industry are assigned a recovery period of seven years. Historically, motorsports racing facilities have been included in this industry and also allowed a seven-year recovery period. However, ambiguities in the law led to questions about whether motorsports racing facilities were correctly categorized. When the Treasury reconsidered the appropriateness of this classification in 2004, Congress made the seven-year treatment mandatory through 2007 with the American Jobs Creation Act (P.L. 108-357). Since 2004, the provision has been extended as part of tax extenders legislation—most recently in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94), which extended the provision through December 31, 2020. Without this provision, motorsports racing facilities would be depreciated over the standard 39-year life.

The tax authorities presumably estimated motorsports racing facilities to have slower depreciation rates than the seven-year life that applies to amusement park facilities. If so, the seven-year-life provision for motorsports racing facilities constitutes a subsidy to the auto racing industry that does not appear to have an obvious justification. Supporters argued that the provision preserves historical treatment and provides a stimulus to business. They also argued that the benefit helps make motorsports facilities more competitive with sports facilities that are often subsidized by state and local governments.

Three-Year Depreciation for Racehorses Two Years or Younger[11]

Racehorses are tangible property, and taxpayers using racehorses in a trade or business must capitalize the cost of purchasing racehorses. The cost can then be recovered through annual depreciation deductions over time. The cost recovery period for racehorses is seven years,

[9] For information on Broadway theatre seating capacity, see the New York Show Tickets website, at http://www.nytix.com/Links/Broadway/broadwaytheatres.html.

[10] IRC §§168(i)(15) and 168(e)(3)(C)(ii).

[11] IRC §168(e)(3)(A).

although racehorses that begin training after age two have a three-year recovery period. Under the temporary provision, this three-year recovery period is extended to all racehorses. In particular, all racehorses placed in service after December 31, 2008, have a three-year recovery period as a result of the Food, Conservation, and Energy Act of 2008 (P.L. 110-246), with provisions subsequently extended. This provision was extended through December 31, 2020, by the Further Consolidated Appropriations Act of 2020 (P.L. 116-94). The industry claims that reducing the recovery period to three years more closely aligns the recovery period with the racing life of a horse. The IRS cost recovery period suggests a longer view. Some racehorses continue in productive activity after their racing career through breeding, as well as having a residual value for resale. Taking those uses into account, a Treasury study estimated an overall economic life of nine years.[12]

This provision does not affect breeders who race their own horses, because they deduct the cost of breeding and thus have no basis (capital investment) in the horses. The provision generally benefits investors who purchase horses.

Accelerated Depreciation for Business Property on an Indian Reservation[13]

The Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66) contained a provision allowing businesses on Indian reservations to be eligible for accelerated depreciation (through a reduction in the applicable recovery periods) as part of an effort to increase investment in Indian reservations. Since its initial temporary enactment, this provision has regularly been extended as part of tax extenders legislation—most recently in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94), which extended the provision through December 31, 2020.

Extending the provision might encourage additional investment on Indian reservations. However, if these provisions' main objective is to improve the economic status of individuals currently living on Indian reservations, it is not clear to what extent this tax subsidy will succeed, because it is not given directly to workers but instead is received by businesses. Capital subsidies may not ultimately benefit workers. It is possible that capital equipment subsidies may encourage more capital-intensive businesses and make workers relatively worse off. In addition, workers would not benefit from higher wages resulting from an employer subsidy if the wage is determined by regulation (the minimum wage) that is set higher than the prevailing market wage.

Economic Development Provisions

Empowerment Zone Tax Incentives[14]

Empowerment Zones (EZs) are federally designated geographic areas characterized by high levels of poverty and economic distress, where businesses and local governments may be eligible to receive federal grants and tax incentives.[15] Since 1993, Congress has authorized three rounds of EZs (1993, 1997, and 1999) with the objective of revitalizing selected economically distressed

[12] U.S. Department of the Treasury, *Report to Congress on the Depreciation of Horses*, March 1990, at https://www.treasury.gov/resource-center/tax-policy/Documents/Report-Depreciation-Horses-1990.pdf.

[13] IRC §168(j)(8).

[14] For related provisions, see IRC §§1391, 1394, 1396, 1397A, and 1397B.

[15] For a list of EZs, see U.S. Department of Housing and Urban Development (HUD), "List of Current Empowerment Zones and Updated Contact Information," at http://portal.hud.gov/hudportal/HUD?src=/program_offices/comm_planning/economicdevelopment/programs/rc/ezcontacts.

communities. EZs are similar to Enterprise Communities (ECs) and Renewal Communities (RCs), which are also federally designated areas for the purposes of tax benefits and grants.

A number of studies have evaluated the effectiveness of the EZ, EC, and RC programs. Government Accountability Office and Department of Housing and Urban Development studies have not found links between EZ and EC designation and improvement in community outcomes.[16] Other research has found modest, if any, effects and called into question these programs' cost-effectiveness. This inability to link these programs to improvements in community-level outcomes should not be interpreted as meaning that the EZ, EC, and RC programs did not aid economic development. The main conclusion from these studies is that the EZ, EC, and RC programs have not been shown to have caused a general improvement in the examined localities' economic conditions. One possible cause for this inability to empirically show the program effects on a large geographic area is that the EZ tax incentives are relatively small. Another possibility is that the EZ tax incentives are targeted at business owners and do not provide direct benefits to workers in EZs.

Six tax incentives are typically related to EZs:[17] (1) local designation of an EZ;[18] (2) increased exclusion of gain;[19] (3) issuance of qualified, tax-exempt zone academy bonds (QZABs) in EZs;[20] (4) EZ employment credits under the Work Opportunity Tax Credit (WOTC);[21] (5) increased expensing under Internal Revenue Code (IRC) Section 179 for businesses located in EZs;[22] and (6) nonrecognition of gain on rollover of EZ investments.[23]

EZs were created by legislation enacted in 1993, and most zones expired at the end of 2009. The provisions were extended in the Protecting Americans from Tax Hikes (PATH) Act of 2015 (P.L. 114-113), which also amended the requirements for tax-exempt enterprise zone facility bonds to treat an employee as a resident of a particular EZ if the employee is a resident of a different EZ, EC, or qualified low-income community. Provisions were extended after 2015, and were last extended through 2020 by the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

For more analysis of EZs, see CRS Report R41639, *Empowerment Zones, Enterprise Communities, and Renewal Communities: Comparative Overview and Analysis*, by Donald J. Marples.

---

[16] For more discussion, see CRS Report R41639, *Empowerment Zones, Enterprise Communities, and Renewal Communities: Comparative Overview and Analysis*, by Donald J. Marples.

[17] For a quick reference chart with a description of each of these provisions, see U.S. Department of Housing and Urban Development (HUD), *Empowerment Zone Tax Incentives Summary Chart*, August 2013, at http://portal.hud.gov/hudportal/documents/huddoc?id=ez_tis_chart.pdf.

[18] IRC §§1391(d)(1)(A)(i) and (h)(2).

[19] IRC §§1202(a)(2) and 1391(d)(1)(A)(i).

[20] IRC §§1394 and 1391(d)(1)(A)(i).

[21] IRC §§1396 and 1391(d)(1)(A)(i). For more information of the WOTC, see CRS Report R43729, *The Work Opportunity Tax Credit*, by Benjamin Collins and Sarah A. Donovan.

[22] IRC §§1397A and 1391(d)(1)(A)(i). For more information on Section 179 expensing, see CRS Report RL31852, *The Section 179 and Section 168(k) Expensing Allowances: Current Law and Economic Effects*, by Gary Guenther.

[23] IRC §§1397B and 1391(d)(1)(A)(i).

American Samoa Economic Development Credit[24]

The American Samoa economy is largely dependent on three sectors: public works and government, tuna canning, and the residual private sector (e.g., tourism and other services).

The American Samoa economic development credit (EDC) is a credit against U.S. corporate income tax in an amount equal to the sum of certain percentages of a domestic corporation's employee wages, employee fringe benefit expenses, and tangible property depreciation allowances for the taxable year with respect to the active conduct of a trade or business within American Samoa. The credit is available to U.S. corporations that, among other requirements, (1) claimed the now-expired possession tax credit (predecessor to the EDC) with respect to American Samoa for their last taxable year beginning before January 1, 2006; or (2) have qualified production activities income after December 31, 2011, in American Samoa (akin to production activities income eligible for Section 199 tax treatment in the United States).[25]

The credit's proponents claim it encourages eligible companies to locate, retain, or expand manufacturing operations in the territory. Media reports suggest the EDC's main beneficiary, thus far, has been StarKist, which has retained its cannery operations in American Samoa.[26]

The EDC was first enacted in the Tax Relief and Health Care Act of 2006 (P.L. 109-432). This version of the EDC was only available to corporations that had previously claimed the possession tax credit, and it originally expired at the end of 2007. It has been extended numerous times. The American Tax Relief Act of 2012 (P.L. 112-240) also expanded the EDC's criteria to include corporations that had not previously claimed the possession tax credit. The provision was most recently extended through 2020 by the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

New Markets Tax Credit[27]

The New Markets Tax Credit (NMTC) was enacted by the Community Renewal Tax Relief Act of 2000 (P.L. 106-554) to encourage investors to invest in low-income communities (LICs) that traditionally lack access to capital. The NMTC is a competitively awarded tax credit overseen by the Community Development Financial Institutions (CDFI) Fund, organized within the Department of the Treasury. For each NMTC round authorized by Congress, the CDFI Fund ranks all requests for NMTC allocation authority and grants awards to those CDEs that score highest. A CDE is a domestic corporation or partnership that is an intermediary vehicle for the provision of loans, investments, or financial counseling in LICs.[28] All taxable investors, such as banks, venture capital firms, and other private investors, are eligible to receive the NMTC.

---

[24] Section 119 of the Tax Relief and Health Care Act of 2006 (P.L. 109-432) as amended by Section 756 of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312), based on the rules of IRC Sections 30A and 936.

[25] See Section 936 of H.Rept. 109-455 and Section 329 of P.L. 112-240. See also JCT, *General Explanation of Tax Legislation Enacted in 2015*, JCS-1-16, March 2016, pp. 196-198, at https://www.jct.gov/publications.html?func=startdown&id=4509. For more information on Section 199, see CRS Report R41988, *The Section 199 Production Activities Deduction: Background and Analysis*, by Molly F. Sherlock.

[26] See "Starkist Am. Samoa Welcomes Tax Credit Extension," Pacific Islands Report, Pacific Islands Development Program at the East-West Center, December 23, 2015, at http://www.pireport.org/articles/2015/12/23/starkist-am-samoa-welcomes-tax-credit-extension.

[27] IRC §45D(f).

[28] Because CDEs serve purposes outside the NMTC, they do not have to be for-profit organizations. However, to receive a NMTC allocation, a CDE must be a for-profit organization.

The NMTC's structure creates incentives for CDEs and private investors to participate in the program. CDEs benefit from the NMTC because they charge fees to their investors for organizing the NMTC application and for structuring the financing for a portfolio of community development projects. The private investors benefit because they receive, each year over seven years, an annual tax credit equal to 5% to 6% of the total amount paid for the stock or capital interest in the CDE that they purchase.[29] Overall, the tax credit amounts to 39% of the cost of the qualified equity investment (less the CDE's fees) as long as the interest in the investment is retained for the entire seven-year period. Thus, even if the community development project funded by the CDE incurs some losses, the value of the tax credit could generate a positive return for the private financers.

Opposition to the NMTC is partly based on the belief that corporations and higher-income investors primarily benefit from the provision or that the NMTC leads to an economically inefficient allocation of resources. For instance, while banks and other investors might benefit directly from the credit, a 2009 study found that the NMTC's benefits to selected low-income communities were modest.[30] The study concluded that poverty and unemployment rates fall by statistically significant amounts in tracts that receive NMTC-subsidized investment relative to similar tracts that do not. From a national economic perspective, the NMTC's impact would be greatest in the case where the investment represents net investment in the U.S. economy rather than a shift in investment from one location to another. Another 2009 study found that corporate NMTC investment represented a shift in investment location, but a portion of individual NMTC investment (roughly $641 million in the first four years of the program from 2001 to 2004) represented new investment.[31]

The NMTC has been extended as a temporary tax provision since 2008, after its initial authorization expired at the end of 2007.[32] In more recent years, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312) extended NMTC authorization through 2011 and permitted a maximum annual amount of qualified equity investments of $3.5 billion. Following several other extensions, the Further Consolidated Appropriations Act of 2020 (P.L. 116-94) extended the provision through 2020 with a maximum allocation authority of $5 billion.

For more information on the NMTC, see CRS Report RL34402, *New Markets Tax Credit: An Introduction*, by Donald J. Marples and Sean Lowry; and CRS Report R42770, *Community Development Financial Institutions (CDFI) Fund: Programs and Policy Issues*, by Sean Lowry.

Other Business Provisions

Indian Employment Tax Credit[33]

The Indian employment tax credit is an incremental credit claimed by employers for qualified wages and health insurance costs. The credit is designed to encourage hiring of certain

[29] For more details, see CRS Report RL34402, *New Markets Tax Credit: An Introduction*, by Donald J. Marples and Sean Lowry.

[30] Matthew Freedman, "Teaching New Markets Old Tricks: The Effects of Subsidized Investment on Low-Income Neighborhoods," *Journal of Public Economics*, vol. 96, no. 11-12 (December 2012), pp. 1000-1014.

[31] Tami Gurley-Calvez et al., "Do Tax Incentives Affect investment? An Analysis of the New Markets Tax Credit," *Public Finance Review*, vol. 34, no. 4 (2009), pp. 371-398.

[32] Given that some of these tax extenders have been passed retroactively, the CDFI Fund has often issued a Notice of Funds Availability (NOFA) for the NMTC in the *Federal Register* despite not having formal authorization of funds.

[33] IRC §45A(f).

individuals—enrolled members of an Indian tribe and their spouses. There are restrictions limiting the benefit to services performed within an Indian reservation for individuals living on or near the reservation.

The Indian employment credit is 20% of the excess of qualified wages and health insurance costs paid by an employer over base-year expenses. The credit is allowed for the first $20,000 in qualified wages and health insurance costs. The base year is 1993, such that the incentive is incremental to 1993 wages and health insurance costs (the base year has not been changed since the credit was enacted). The credit is not available for wages paid to an employee whose total wages exceed $30,000, as adjusted for inflation ($50,000 in 2019). The employer must reduce the deduction for wages by the amount of the credit.

The Indian employment credit was first enacted in 1993, as part of the Omnibus Reconciliation Act of 1993 (P.L. 103-66). It was initially scheduled to expire at the end of 2003, but has been regularly extended, often retroactively. Past extensions of the Indian employment credit have extended the termination date without updating the base year. Some have proposed updating the base year, in an effort to (1) eliminate the need for taxpayers to maintain tax records dating back to 1993 and (2) restore the credit's incremental design.[34] The most recent extension was through 2020 in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

Extending the Indian employment credit might encourage additional hiring of Indian tribe members and their spouses. Although the Indian employment credit may not increase overall employment on or near Indian reservations, it might increase employment among tribe members.

Mine Rescue Team Training Credit[35]

Taxpayers that employ miners in underground mines located in the United States may be able to claim a tax credit for mine rescue team training expenses. The credit amount is limited to the lesser of (1) 20% of training program costs per employee (including wages paid to the employee while in training) or (2) $10,000. For a taxpayer to claim the credit for training provided to an employee, the employee must be a full-time miner who is eligible to serve as a mine rescue team member.

The mine rescue team training credit was enacted in the Tax Relief and Health Care Act of 2006 (P.L. 109-432). It was initially scheduled to be effective for 2006, 2007, and 2008. It has subsequently been extended as part of tax extenders legislation, most recently through 2020 in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

The mine rescue team training credit was enacted at the end of 2006, following the high-profile mining accident at Sago Mine. There was an uptick in coal mining fatalities in 2006—47 fatalities were reported (12 were a result of the Sago Mine disaster).[36] From 2007 through 2019, coal mining fatalities averaged 20 per year. During this period, fatalities were highest in 2010, reflecting the Upper Big Branch Mine disaster, where there were 29 fatalities. In the year with the lowest number of fatalities, 2016, there were 8. In 2019, there were 11 coal mining fatalities. Coal mining fatalities have generally been trending downward over time. In recent years, some of this

[34] See, for example, Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals*, February 2016, pp. 39-41, at http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2017.pdf.

[35] IRC §45N(e).

[36] U.S. Department of Labor, Mine Safety and Health Administration, *Coal Fatalities for 1900 through 2019*, at https://arlweb.msha.gov/stats/centurystats/coalstats.asp.

might be explained by a decline in coal production and the decline in the number of coal miners. The fatality rate, however, has also tended to decline over time.

A credit for mine rescue team training can encourage mine operators and employers to invest in additional training. The credit can also reduce the cost of complying with federal regulations regarding mine rescue team training.[37] Federal regulations are the government's primary policy instrument governing coal mine safety, with tax incentives playing a small role.[38]

Employer Tax Credit for Paid Family and Medical Leave[39]

The employer credit for paid family and medical leave (PFML) can be claimed by employers providing paid leave (wages) to employees under the Family and Medical Leave Act of 1993 (FMLA; P.L. 103-3). The credit can be claimed for wages paid during tax years that begin in 2018, 2019, and 2020.

The credit amount is equal to up to 25% of PFML wages paid to qualifying employees.[40] The credit can only be claimed for PFML provided to certain employees with incomes below a fixed threshold.[41] For credits claimed in 2019, employee compensation in 2018 cannot have exceeded $72,000. The amount of PFML wages for which the credit is claimed cannot exceed 12 weeks per employee per year. Further, all qualifying employees must be provided at least two weeks of PFML for an employer to be able to claim the credit. Tax credits cannot be claimed for leave paid by state or local governments, or for leave that is required by state or local law. To claim the credit, an employer must have a written family and medical leave policy in effect. The policy cannot exclude certain classifications of employees, such as unionized employees.

The employer credit for paid family and medical leave was added to the IRC in the 2017 tax revision (P.L. 115-97; commonly referred to as the Tax Cuts and Jobs Act). Initially, the credit was effective for wages paid in 2018 and 2019. The credit was extended for one year, through 2020, by the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

Providing a tax credit for employers that provide PFML should, on the face of it, tend to increase access to this benefit. How effective the credit will be at achieving this goal remains an open question. Employers may provide PFML to qualified employees for a number of reasons; attracting high-quality talent might be one. If most of the credit's beneficiaries are employers that would have provided PFML without the credit, then the credit is not a particularly efficient mechanism for increasing PFML. There is also the possibility that employers choose to substitute credit-eligible PFML for other forms of leave. An employer could reduce the amount of paid sick, personal, or vacation time off, knowing that employees use this time for paid family and medical leave purposes. If other benefits are scaled back in favor of tax-preferred FMLA leave, employees may not be better off.

---

[37] More on federal requirements for mine rescue team training can be found on the U.S. Department of Labor, Mine Safety and Health Administration website, at https://www.msha.gov/training-education/mine-rescue-training.

[38] 30 C.F.R. §49. For background information, see CRS Report RL34429, *Coal Mine Safety and Health*. (This out-of-print CRS report is available to congressional clients from the authors upon request.)

[39] IRC §45S.

[40] The credit rate increases from 12.5% to 25% ratably as leave wages increase from 50% to 100% of wages normally paid.

[41] A qualifying employee is one who, in the preceding year, did not have compensation in excess of 60% of the amount applicable for a highly compensated employee under the nondiscrimination requirements rules for qualified retirement plans (IRC §414(q)(1)(B)).

For more information, see CRS In Focus IF11141, *Employer Tax Credit for Paid Family and Medical Leave*, by Molly F. Sherlock.

Work Opportunity Tax Credit[42]

The work opportunity tax credit (WOTC) is a nonrefundable wage credit intended to increase job opportunities for certain categories of disadvantaged individuals. The WOTC reduces the cost of hiring specified groups of disadvantaged individuals. WOTC-eligible hires include members of families receiving Temporary Assistance to Needy Families (TANF) benefits, certain members of families receiving food stamp benefits, ex-felons, and certain veterans.

For most eligible hires that remain on a firm's payroll at least 400 hours, an employer can claim an income tax credit equal to 40% of wages paid during the worker's first year of employment, up to a statutory maximum. For most WOTC-eligible hires, the wage maximum is $6,000, for a maximum credit of $2,400. For eligible veterans, the maximum eligible wage varies between $6,000 and $24,000, depending on the veteran's characteristics and work history. Eligible summer youth hires' maximum wage to which the credit can be applied is $3,000. A credit equal to 25% of a qualified worker's wages is available for eligible hires that remain employed for at least 120 hours, but fewer than 400 hours.

The WOTC was created as part of the Small Business Job Protection Act of 1996 (P.L. 104-188). The WOTC evolved from an earlier tax credit designed to increase employment among targeted groups, the Targeted Jobs Tax Credit (TJTC), which was available from 1978 through 1994. When first enacted, the WOTC was scheduled to expire on October 1, 1997. Since 1997, the WOTC has been expanded, modified, and regularly extended. In several instances, the WOTC was allowed to lapse before being retroactively reinstated. It was most recently extended through 2020 in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

The WOTC is designed to encourage employers to hire more disadvantaged individuals by compensating for potential higher training costs and possible lower productivity. Because the credit is focused on hiring from targeted groups, and not net job creation, it is not necessarily intended to create new jobs or promote recovery in labor markets.[43] Studies evaluating the credit have examined whether it increases job opportunities for targeted disadvantaged individuals, and whether the WOTC is a cost-effective policy measure for achieving this objective.

Early evidence on the WOTC suggested that although the credit did offset part of the cost of recruiting, hiring, and training WOTC-eligible employees, it had a limited effect on companies' hiring decisions.[44] More recent studies have found that the WOTC provided benefits to certain groups: increasing the wage income of disabled veterans and increasing employment among long-term welfare recipients, for example. Researchers have also explored whether the credit causes employers to "churn" their workforce to take advantage of the credit, replacing currently credit-ineligible workers with credit-certified workers. Evidence of this behavior has not been found.

---

[42] IRC §51(c)(4).

[43] Kenneth A. Couch, Douglas J. Besharov, and David Neumark, "Spurring Job Creation in Response to Severe Recessions: Reconsidering Hiring Credits," *Journal of Policy Analysis and Management*, vol. 32, no. 1 (Winter 2013), pp. 142-171.

[44] For an overview of the empirical literature on the WOTC, see U.S. Congress, Senate Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, committee print, prepared by Congressional Research Service, 113th Cong., December 2014, S. Prt. 113-32, pp. 753-762, http://www.crs.gov/Products/CommitteePrint/CP10001.pdf.

For more information on the WOTC, see CRS Report R43729, *The Work Opportunity Tax Credit*, by Benjamin Collins and Sarah A. Donovan.

Look-Through Treatment of Payments Between Related Controlled Foreign Corporations[45]

The temporary look-through rules were originally enacted in the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222), for 2006 through 2008, and subsequently extended. These rules effectively allow U.S. corporations to reduce tax paid by allowing them to shift the income of certain foreign subsidiaries in high-tax countries into a lower-taxed foreign subsidiary.

Depending on its source, income earned abroad by foreign-incorporated subsidiaries of U.S. parents is taxed at full rates, not taxed at full rates, or not taxed at all. Tax rules require passive income (such as interest income) and certain types of payments that can be easily manipulated to reduce foreign taxes to be taxed at the full rate (21% for a corporate shareholder) if earned by controlled foreign corporations (CFCs).[46] This income is referred to as Subpart F income, reflecting the part of the tax code where treatment is specified. Credits against the U.S. tax imposed are allowed for any foreign taxes paid on this income, and are applied on an overall basis (so that unused foreign taxes in one country can offset taxes paid on income in another country). Other income earned abroad by CFCs is subject to the global intangible low-taxed income (GILTI) provision, which taxes this foreign-source income at half the corporate tax rate (10.5%), after allowing a deduction for a deemed return of 10% on tangible assets. Credits are allowed for 80% of foreign taxes paid. This GILTI rate is scheduled to rise to 13.125% after 2025.

Thus, some income (Subpart F) is taxed at the full rate, some income (GILTI) is taxed at partial rates, and some income (the deemed return from tangible assets) is not taxed. (For a more extensive discussion of international tax rules, see CRS Report R45186, *Issues in International Corporate Taxation: The 2017 Revision (P.L. 115-97)*, by Jane G. Gravelle and Donald J. Marples.)

Unless an exception applies, Subpart F income includes dividends, interest, rent, and royalty payments between related firms. These items of income are subject to Subpart F because affiliated firms can use them to shift income and avoid taxation. For example, without Subpart F a U.S. parent's subsidiary (first-tier subsidiary) in a country without taxes (e.g., the Cayman Islands) could lend money to its own subsidiary (second-tier subsidiary) in a high-tax country. The interest payments would be deductible in the high-tax country, but no tax would be due in the no-tax country. Thus, an essentially paper transaction would shift income out of the high-tax country. A similar effect might occur if an intangible asset were transferred to the no-tax subsidiary, and then licensed in exchange for a royalty payment by the high-tax subsidiary. Subpart F taxes this income at full rates.

Methods of avoiding Subpart F taxation were made easier in 1997, when U.S. entity classification rules (to be a corporate or noncorporate entity) were simplified to allow checking a box on a form. These "check-the-box" regulations provided a way to avoid treatment of payments as Subpart F income under certain circumstances by allowing firms to elect treatment as an unincorporated entity. They were originally intended to simplify classification issues for domestic

[45] IRC §954(c)(6).

[46] A CFC is 50% or more controlled by U.S. parents who each have at least 10% ownership. Many CFCs are wholly owned by one U.S. parent corporation. CFCs can be owned by individuals as well as corporations, but individual shareholders are not eligible for benefits such as the GILTI deduction. Individuals can elect corporate treatment, however.

firms and the IRS, but their usefulness in international tax planning quickly became evident. The Treasury issued regulations in 1998 to disallow their use to avoid Subpart F, but withdrew them after protests from firms and some Members of Congress.

In the example above, if the high-tax subsidiary is not a direct subsidiary of the U.S. parent but is a subsidiary of the Cayman Islands subsidiary (i.e., a second-tier subsidiary), the Cayman Islands (first-tier) subsidiary can elect to treat the high-tax subsidiary as if it were a pass-through entity. This treatment would effectively combine the two subsidiaries into a single firm. This outcome can be achieved simply by checking a box, making the high-tax subsidiary a disregarded entity under U.S. law. Because there are no separate firms, no income is recognized by the Cayman Islands firm, although the high-tax subsidiary (second tier) is still a corporation from the point of view of the foreign jurisdiction in which it operates and can deduct interest in the high-tax jurisdiction.

The look-through rules expand the scope of check-the-box. The rules were originally enacted in the Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222), for 2006 through 2008, and subsequently extended, most recently through 2020 in the Further Consolidated Appropriations Act of 2020 (P.L. 116-94). The check-the-box rules do not work in every circumstance. For example, if the related firms do not have the same first-tier parent, check-the-box does not apply. In some cases, because of foreign countries' rules about corporate and noncorporate forms, the check-the-box regulations' classification of some entities as per se corporations make this planning unavailable. In addition, other undesirable tax consequences (from the firm's point of view) could occur as a side effect of check-the-box. The look-through rule effectively puts this check-the-box type of planning into the tax code, rather than implementing it as a regulation (which could be altered without legislation), but disconnects it from the check-the-box regulations' creation of a disregarded entity. Related firms do not have to have the parent-child relationship; they can be otherwise related as long as they are under common control.

The main argument against the look-through rules (and check-the-box as well) is that they undermine Subpart F's purpose, which is to prevent firms from using passive and easily shifted income to avoid taxation. The main argument for the provision is to allow firms the flexibility to redeploy earnings from one location to another without having U.S. tax consequences (foreign tax rules are unchanged). Firms could, for example, accomplish much of the treatment of look-through rules (even in the absence of check-the-box), but that may involve complex planning and inconvenience. An argument can also be made that in some cases (for example, with the payment of interest), the profit shifting is not harming the U.S. Treasury, but rather reducing taxes collected by foreign governments, as income is shifted out of high-tax countries into low-tax ones. Some might view this last argument as a "beggar-thy-neighbor" argument because it facilitates U.S. firms in using tax planning to reduce taxes paid to other countries.

Provisions Modifying the Excise Taxes on Wine, Beer, and Distilled Spirits[47]

The temporary provisions modifying excise taxes on alcoholic beverages were originally enacted through 2019 in the 2017 tax revision (the Tax Cuts and Jobs Act, P.L. 115-97). The first provision applies to beer, wine, and distilled spirits broadly. The provisions that apply only to beer, wine, or distilled spirits are discussed separately below.

In general, the uniform capitalization (UNICAP) rules require some costs that would otherwise be immediately deductible (such as interest and overhead) to be added to inventory or to the cost of

[47] IRC §§263A, 5041. 5051, 5414.

property and deducted in the future when goods are sold or assets depreciated. In the case of interest costs, the rules apply only if the asset is long-lived or has a production period over two years or a production period over one year and a cost of more than $1 million. The production period includes any customary aging period. A temporary modification to the UNICAP rules exempts the aging periods for beer, wine, and distilled spirits from the production period for the UNICAP interest capitalization rules, thus leading to shorter production periods.

Beer

Absent the temporary excise tax modification provisions, the excise tax rate on beer producers is $18 per barrel (31 gallons), and small brewers that domestically produce no more than 2 million barrels annually are subject to a rate of $7 per barrel on the first 60,000 barrels. The temporary provision reduces the rate for small brewers (producing no more than 2 million barrels) to $3.50 per barrel on the first 60,000 barrels and $16 per barrel on the remaining production. Beer importers and large producers meeting certain requirements may also be eligible for the reduced rate of taxation. For all other producers or importers, the excise tax rates are $16 per barrel on the first 6 million barrels.

The tax on beer is due when the beer is removed from the brewery for sale. Beer can be transferred between breweries that are commonly owned (and released from customs) without paying the tax (although tax would be paid on the eventual sale). The temporary provision also allows transfer without payment of tax to an unrelated brewer if the transferee accepts responsibility for paying the tax.

Wine

Excise taxes are imposed at different rates on wine, depending on the wine's alcohol content and carbonation levels. Still wines are taxed at $1.07 per wine gallon (w.g.) if they are 14% alcohol or less, $1.57/w.g. if they are 14% to 21% alcohol, and $3.15 per w.g. if they are 21% to 24% alcohol. Naturally sparkling wines are taxed at $3.40 per w.g. and artificially carbonated wines are taxed at $3.30 per w.g.

Absent the temporary provisions, up to a $0.90 credit against excise tax liability ($0.056 per w.g. for hard cider) may be available for the first 100,000 w.g. removed by a small domestic winery producing not more than 150,000 w.g. per year. The per wine gallon tax credit rate is phased out on production in excess of 150,000 w.g. for wineries producing not more than 250,000 w.g. per year. This small winery credit does not apply to sparkling wine.

The temporary provisions modify the credit for small domestic wineries to allow it to be claimed by domestic and foreign producers, regardless of the gallons of wine produced. The credit is also made available to sparkling wine producers. Also, a $1.00 credit against excise tax liability may be available for the first 30,000 w.g. removed annually by any eligible wine producer or importer. The credit is reduced to $0.90 on the next 100,000 w.g., and $0.535 on the next 620,000 w.g. In contrast to permanent law, this credit is not phased out based on production. For hard cider, the credit rates, above, are adjusted to $0.062 per gallon, $0.056 per gallon, and $0.033 per gallon, respectively.

Mead is taxed according to wine excise tax rates depending on its alcohol and carbonation content. Naturally sparkling wines are taxed at $3.40 per w.g. and artificially carbonated wines taxed at $3.30 per w.g. Under the temporary provision, mead and certain sparkling wines are to be taxed at the lowest rate applicable to still wine of $1.07 per wine gallon. Mead contains not more than 0.64 grams of carbon dioxide per hundred milliliters of wine, which is derived solely from honey and water, contains no fruit product or fruit flavoring, and contains less than 8.5% alcohol.

The sparkling wines eligible to be taxed at the lowest rate contain no more than 0.64 grams of carbon dioxide per hundred milliliters of wine, which are derived primarily from grapes or grape juice concentrate and water, which contain no fruit flavoring other than grape, and which contain less than 8.5% alcohol.

Distilled Sprits

Producers and importers of distilled spirits are taxed at a rate of $13.50 per proof gallon (ppg) of production. Under the temporary provision, the tax rate is lowered to $2.70 ppg on the first 100,000 proof gallons, $13.34 ppg for proof gallons in excess of that amount but below 22,130,000 proof gallons, and $13.50 ppg for amounts thereafter. The provision contains rules to prevent members of the same controlled group from receiving the lower rate on more than 100,000 proof gallons of distilled spirits.

Distilled spirits are taxed when removed from the distillery, or, in the case of an imported product, from customs custody or bonded premises. Bulk distilled spirits may be transferred in bond between bonded premises without being taxed, but may not be transferred in containers smaller than one gallon. The temporary provision allows transfer of spirits in approved containers other than bulk containers without payment of tax.

Provisions Expiring in 2021, 2022, or 2023

12.5% Increase in Annual LIHTC Authority[48]

The low-income housing tax credit (LIHTC) program, which was created by the Tax Reform Act of 1986 (P.L. 99-514), is the federal government's primary policy tool for the development of affordable rental housing. LIHTCs are awarded to developers to offset the cost of constructing rental housing in exchange for agreeing to reserve a fraction of rent-restricted units for lower-income households. Although it is a federal tax incentive, the program is primarily administered by state housing finance agencies (HFAs) that award tax credits to developers.

Authority for states to award tax credit is determined according to each state's population. In 2020, the amount of tax credits a state can award is equal to $2.8125 per person, with a minimum small population state authority of $3,217,500. These figures reflect a temporary increase in the amount of credits each state received for 2018-2021 as a result of the 2018 Consolidated Appropriations Act (P.L. 115-141). The increase is equal to 12.5% above what states would have received absent P.L. 115-141, and is in effect through 2021.

For more information on the LIHTC, see CRS Report RS22389, *An Introduction to the Low-Income Housing Tax Credit*, by Mark P. Keightley.

Computation of Adjusted Taxable Income Without Regard to Any Deduction Allowable for Depreciation, Amortization, or Depletion[49]

Prior to the 2017 tax revision (the Tax Cuts and Jobs Act, P.L. 115-97), the deduction for net interest was limited to 50% of adjusted taxable income (income before taxes; interest deductions;

[48] IRC §42(h)(2)(I).

[49] IRC §163(j).

and depreciation, amortization, or depletion deductions) for firms with a debt-equity ratio above 1.5. Interest above the limitation could be carried forward indefinitely. The revision limited deductible interest to 30% of adjusted taxable income for businesses with gross receipts greater than $25 million. The provision also has an exception for floor plan financing for motor vehicles. Businesses providing services as an employee and certain regulated utilities are excepted from this new limit. Also, certain real property and farming businesses can elect out of this limit but must adopt a slower depreciation method for real property or farming assets. The restrictions on interest, called *thin capitalization rules*, were partially enacted to address concerns about large multinational businesses locating borrowing in the United States to shift profits out of the United States and to foreign, lower-tax, jurisdictions.

Under prior law and the temporary provisions of the 2017 tax revision, this interest limit applies to earnings (income) before interest, taxes, depreciation, amortization, or depletion (referred to as EBITDA). After 2021, the 2017 tax revision changes the measure of income to earnings (income) before interest and taxes (referred to as EBIT). Because EBIT is after the deduction of depreciation, amortization, and depletion, it results in a smaller base and thus a smaller amount of eligible interest deductions. The temporary broader base (EBITDA), which expires in 2021, allows more interest deductions. The current, more generous rules for measuring the adjusted taxable income base are more beneficial to businesses with depreciable assets, although affected businesses might be able to avoid some of the change in the deduction rules by leasing assets from financial institutions, such as banks, that generally have interest income.

This change in base is projected to have a significant revenue consequence: the Joint Committee on Taxation estimated the revenue gain from the provision to increase from $19.2 billion in FY2021 to $30.2 billion in FY2023, when the change is fully in effect, an increase of more than $10 billion.[50] This revenue change suggests the cost of allowing the broader measure of income (EBITDA) through 2021 is around $10 billion annually.

For additional discussion of the interest limitation, see CRS Report R45186, *Issues in International Corporate Taxation: The 2017 Revision (P.L. 115-97)*, by Jane G. Gravelle and Donald J. Marples.

The Rum Cover Over[51]

Under permanent law, the excise tax on rum is $13.50 per proof gallon and is collected on rum produced in or imported into the United States. Under permanent law, $10.50 per proof gallon of imported rum is transferred or "covered over" to the Treasuries of Puerto Rico (PR) and the United States Virgin Islands (USVI). Temporary provisions have increased the transfer amount to $13.25. The law does not impose any restrictions on how PR and USVI can use the transferred revenues. Both territories use some portion of the revenue to promote and assist the rum industry.

The cover-over provisions for rum extend as far back as 1917 for PR and 1954 for USVI. Originally, the full amount of the tax was covered over; however, the Deficit Reduction Act of 1984 (P.L. 98-369) limited the cover over to $10.50 when the federal tax rates were increased to $12.50. The cap was intended to address the question of whether the rebates were proper given the lack of rebates to the states. The Omnibus Budget Reconciliation Act of 1993 (OBRA93; P.L. 103-66) temporarily increased the cap to $11.30 for five years, in a law that also reduced another benefit to the possessions (the possessions tax credit). When this increase expired, the cap was

---

[50] Joint Committee on Taxation, *Estimated Budget Effects of the Conference Agreement for H.R. 1, the "Tax Cuts and Jobs Act,"* December 18, 2017, JCX-67-17.

[51] IRC §7652(e).

increased to $13.25, and it has subsequently been extended, most recently through 2021 by the Bipartisan Budget Act of 2018 (P.L. 115-123).

For additional information on the rum cover over see CRS Report R41028, *The Rum Excise Tax Cover-Over: Legislative History and Current Issues*, by Steven Maguire.

Credit for Certain Expenditures for Maintaining Railroad Tracks[52]

Qualified railroad track maintenance expenditures paid or incurred in a taxable year by eligible taxpayers qualify for a 50% business tax credit. The credit is limited to $3,500 multiplied by the number of miles of railroad track owned or leased by an eligible taxpayer. Qualified railroad track maintenance expenditures are amounts, which may be either repairs or capitalized costs, spent to maintain railroad track (including roadbed, bridges, and related track structures) owned or leased as of January 1, 2005, by a Class II or Class III (regional or local) railroad. Eligible taxpayers are smaller (Class II or Class III) railroads and any person who transports property using these rail facilities or furnishes property or services to such a person.

The taxpayer's basis in railroad track is reduced by the amount of the credit allowed (so that any deduction of cost or depreciation is only on the cost net of the credit). The credit cannot be carried back to years before 2005. The credit is allowed against the alternative minimum tax. The amount eligible is the gross expenditures, not accounting for reductions such as discounts or loan forgiveness.

The provision was enacted in the American Jobs Creation Act of 2004 (P.L. 108-357) and extended numerous times. The provision relating to discounts was added by the Tax Relief and Health Care Act of 2006 (P.L. 109-432). The credit was allowed against the alternative minimum tax by the Emergency Economic Stabilization Act of 2008 (P.L. 110-343). It was most recently extended through 2022 by the Further Consolidated Appropriations Act of 2020 (P.L. 116-94).

This provision substantially lowers the cost of track maintenance for the qualifying short-line (regional and local) railroads, with tax credits covering half the costs for those firms and individuals with sufficient tax liability. Class II and III railroads account for 32% of the nation's freight rail miles.[53] These regional railroads are particularly important in providing transportation of agricultural products.

Although no rationale was provided when the credit was introduced, sponsors of earlier freestanding legislation and industry advocates indicated that the purpose was to encourage the rehabilitation, rather than the abandonment, of short-line railroads. These railroads were spun off in the deregulation of railroads in the early 1980s. Advocates also indicated that this service is threatened by heavier 286,000-pound cars that must be used to connect with longer rail lines. They also suggested that preserving these local lines would reduce local truck traffic. There was also some indication that a tax credit was thought to be more likely to be achieved than grants.

The arguments stated by industry advocates and sponsors of the legislation are also echoed in assessments by the Federal Railroad Administration (FRA), which indicated the need for rehabilitation and improvement, especially to deal with heavier cars. The FRA also suggested that these firms have limited access to bank loans.

[52] IRC §45G(f).

[53] Association of American Railroads, *Overview of America's Freight* Railroads, June 2019, https://www.aar.org/wp-content/uploads/2018/08/Overview-of-Americas-Freight-RRs.pdf.

Author Contact Information

Molly F. Sherlock, Coordinator
Specialist in Public Finance
/redacted/@crs.loc.gov , 7-....

Sean Lowry
Analyst in Public Finance
/redacted/@crs.loc.gov, 7-....

Jane G. Gravelle
Senior Specialist in Economic Policy
/redacted/@crs.loc.gov, 7-....

Donald J. Marples
Specialist in Public Finance
/redacted/@crs.loc.gov, 7-....