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INSIGHT

Targeted Tax Relief for Industries Impacted by the Coronavirus: Selected Policy Issues

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One of the policy options being considered to minimize the damage to the U.S. economy from the domestic spread of the coronavirus is tax relief targeted at industries that have experienced substantial drops in revenue. To date, growing numbers of cruise lines, airlines, hotels, restaurants, retailers, and energy producers seem to have been hit the hardest by the economic impact of the virus. Depending on what happens to the spread of the coronavirus within the United States in coming weeks, other industries could be similarly affected. The prospect of a prolonged domestic coronavirus outbreak raises concerns about the solvency of severely affected companies and the job security of their employees. This is a particular concern for smaller firms. Without lines of credit, many of them may find it difficult to stay in business.

According to the Congressional Budget Office, fiscal policies for reviving a slumping economy can be evaluated on the basis of their timing and cost-effectiveness. Timing refers to the period when a fiscal stimulus would have the greatest effect. Cost-effectiveness refers to the cumulative growth in output and jobs created by a particular stimulus measure per dollar of budgetary cost. Timely and cost-effective fiscal stimulus measures are seen as recommended ways to boost an economy at a relatively low revenue cost.

The same considerations may be useful in assessing the potential benefits from proposals to provide federal tax relief for industries directly affected by the coronavirus pandemic. Lawmakers may want to focus on proposals that would be likely to deliver the maximum benefit when it is most needed, at a relatively low revenue cost.

Tax Policy Options

There are several policy options for granting federal tax relief to U.S. industries that have been hit hard by the coronavirus pandemic. One option is to defer payment of federal employment, income, and excise taxes by eligible companies for a period that coincides with the time it takes for the coronavirus outbreak

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to run its course. Most companies are required to deposit the federal income, Medicare, and Social Security taxes they withhold from employees' paychecks biweekly or monthly with the U.S. Treasury Department. At the moment, it is unclear how long it will take for the current outbreak to run its course.

Another option is to provide a refundable tax credit for affected companies, up to a certain amount. This would benefit firms with net operating losses—as well as those with reduced profits—because of the pandemic. Both sets of firms could claim the full amount of the credit. The timing of this option may be problematic, if, as is typically the case under current law, the credit could be claimed only at the end of a company's tax year. The credit could be given in advance, as is the case with the refundable health insurance premium tax credit under the Affordable Care Act (P.L. 111-148).

A third option is to allow affected companies to carry back any net operating loss (NOL) to offset taxes paid in previous years, producing an immediate refund. Before the 2017 tax revision (P.L. 115-97), companies could carry their NOLs back up to two years as an offset to previous profits, or forward up to 20 years as a deduction against future profits. There was no limit on the amount of the NOL a company could use for either purpose. Under P.L. 115-97, however, NOLs may not be carried back, but they may be carried forward indefinitely; use of the NOL deduction is capped at 80% of a company's taxable income.

Targeted tax relief is unlikely to keep businesses operating and workers employed if public health measures to contain the virus's spread (e.g., self-quarantines and sheltering-in-place) cause demand for their products and services to decline sharply. The same outcome could happen when a shortage of parts and supplies makes it impossible for them to stay in business. In this case, tax relief may need to be coupled with federal loans, loan guarantees, or grants to prevent an increase in business failures in affected industries. Numerous small businesses may be especially vulnerable to insolvency during the current coronavirus outbreak, as they have limited or no access to bank loans.

Policy Issues

Granting targeted tax relief to businesses hit hard by the economic effects of the coronavirus raises several policy issues. One is where to draw the line between eligible and ineligible companies. If a major hotel chain, for instance, were to qualify for a refundable tax credit, would that credit also be available to firms providing online room rentals (e.g., Airbnb)? What about companies that supply food, laundry, security, and cleaning services to the hotel chain as contractors? Should the tax relief be extended to lawyers and accountants who derive much of their income from work they do for the hotel chain? In crafting targeted tax relief for industries affected by the virus, Congress may have to deal with the question of how far downstream in the supply chain tax relief should be available.

Another issue concerns the eligibility criteria for any tax relief. Should the benefit apply only to companies whose revenue falls by 10%, or 20%, or some other percentage? Or should the benefit be targeted instead at profits? Should a company have to demonstrate to the Internal Revenue Service that its revenue or profit declines or operating losses were due to the coronavirus? If so, how would it do so? Should the tax relief be limited to small companies only? If so, how should a small company be defined?

There is no certainty that whatever cash infusion impacted companies receive from targeted tax benefits would filter down to employees. Owners could be the biggest beneficiaries. Such an outcome would do little to maintain or grow aggregate demand for goods and services.