A Practical Challenge to Stand-Alone Corporate Tax Reform

By Donald B. Marron

Leaders in both parties appear to favor revenue-neutral corporate tax reform that would lower today’s 35 percent tax rate while slashing corporate tax breaks. Efforts to reform the individual income tax, in contrast, remain mired in disagreements over revenue targets and marginal tax rates. Many observers thus wonder whether policymakers should pursue corporate tax reform by itself, separate from any individual reforms.

One practical challenge to stand-alone corporate reform is that many corporate tax breaks also apply to noncorporate businesses, which are taxed under the individual income tax. Efforts to broaden the corporate base could therefore have significant effects on individual income taxes, making it difficult to pursue corporate reform separately.

The Joint Committee on Taxation recently identified about $1.3 trillion in income tax expenditures in 2013.1 The vast majority, more than $1.1 trillion, operate through the individual income tax. Of those, more than $1 trillion have no link to corporate income taxes. The mortgage interest deduction and the exclusion of employer-provided health insurance, for example, operate exclusively through the individual income tax. As a result, it’s possible to talk about major, base-broadening reform of the individual income tax without worrying much about collateral effects on the corporate income tax.

The reverse is not true for efforts at corporate tax reform. Partnerships, S corporations, sole propri-

1Joint Committee on Taxation, “Estimates of Federal Tax Expenditures for Fiscal Years 2012-2017,” JCS-1-13 (Feb. 1, 2013). The JCT lists the static revenue cost of each individual and corporate tax expenditure, but it does not report an aggregate figure. Adding the separate provisions, as done here, is imprecise because it does not capture how the provisions interact. Nevertheless, it provides useful, albeit approximate, information about how the provisions overlap.