Corporate Welfare in the Federal Tax System

By: Ryan Riebe - February 21, 2013

Frequently, entitlement reform is discussed among policymakers as a way to reduce government spending, but the entitlement reform discussed often concerns individual entitlements, not those directed toward corporations. A recent examination of the federal tax code by the Cato Institute's Tad DeHaven found that each year corporate welfare in the tax code cost taxpayers nearly $100 billion. In some cases, corporate welfare is used by the federal government to fund activities that would not otherwise occur in the private sector, simply because these activities are not economically viable without government subsidies. Not all examples of corporate welfare fit into this category however, as some corporate tax breaks are also designed to subsidize activities that would occur naturally, without government assistance. For either case, corporate welfare is nothing more than the government choosing winners and losers in the private sector.

One place where corporate tax incentives are directed is toward the expensing of research and experimental expenditures, where an estimated $4.9 billion will be spent by the federal government during fiscal year 2013. According to the Internal Revenue Service, research and experimental expenditures are defined as "reasonable costs you incur in your trade or business for activities intended to provide information that would eliminate uncertainty about the development or improvement of a product." There is no reason why this research needs to be subsidized by the federal government, and the government decreasing the tax burden of particular companies who devote resources toward research and experiments does nothing more than allow the government to show favoritism to particular corporations over others.

Corporate welfare is also highly prevalent in the energy industry, with subsidies available to energy companies who produce electricity from renewable sources. Among the types of energy whose production is subsidized by the federal government are wind energy, closed and open-loop biomass, geothermal energy, hydropower, solar power, small irrigation power, and municipal solid waste. Credits for each of the aforementioned methods of electricity production generally range anywhere from 1.1 cents to 2.2 cents per kilowatt hour. Of these methods of energy production, wind energy producers are the largest recipients of corporate welfare, scheduled to receive an estimated $1.4 billion in tax credits for electricity production during the 2013 fiscal year.

Often these subsidies do very little to offset the differences between the levelized costs associated with renewable energy as compared to the costs associated with the production of electricity from a source like natural gas. For example, the levelized cost (the net cost to install and operate an energy system divided by its expected life-time energy output) of generating electricity from natural gas is an average of 6.3 cents per kilowatt hour, as compared to generating energy from solar sources, which has an average levelized production cost of 21.1 cents per kilowatt hour. While a subsidy for the production of electricity from solar power does reduce the levelized cost of solar energy, it does not make the price of solar power competitive with the cost of electricity generated from sources like natural gas or coal. If the mass production of solar powered electricity were a realistic option for electricity production in the United States, the federal government would not need to subsidize it, or other forms of renewable energy production. Instead, renewable energy credits are merely an example of the government using corporate welfare to create an un-level playing field in the American energy industry.

In addition to subsidizing the production of electricity from renewable sources, the federal government also offers a tax credit to companies who install specifically designated equipment for the generation of renewable energy. During the 2013 fiscal year, these corporate tax credits are estimated to cost taxpayers an estimated $400 million on top of the already heavy burden of subsidies for the production of electricity from renewable resources. By subsidizing the installation of equipment to generate electricity from renewable sources, the government is once again offering corporate welfare to companies who wish to use a form of energy that is too costly to happen without government support in the private sector.

A final example of corporate welfare (for this blog, as many other examples of government sponsored corporate welfare exist) is the subsidization of corporate contributions to employee stock ownership plans. For the 2013 fiscal year, corporate deductions of employer contributions to employee stock ownership plans as business expenses will cost the federal government an estimated $1 billion. These corporations could easily finance the distribution of stock to their employees without taxpayer assistance, yet the federal government feels the need to involve themselves in employee stock ownership programs unnecessarily, the reason why this particular tax deduction is merely an arm of big government promoting corporate welfare.

The previous examples of corporate welfare as subsidized by American taxpayers through the federal government are by no means comprehensive, nor all-inclusive. Each year, the federal government spends nearly $100 billion of the taxpayers' money to support corporations, who can easily support themselves, and these corporations are more than happy to accept "free" taxpayer money. If we want to solve our government's fiscal problems, ending unnecessary corporate welfare would be a good place to start.