The U.S. corporation operates on cash flow. Accounting conventions tell us that taxes should be charged to the period giving rise to their liability—usually, in practice, the fiscal quarter—but they do not tell us when they are or should be paid.

U.S. corporate treasurers are not fools, with taxes due, on average, seven or eight months after their liability arises, they tell themselves, "Why fund the money? Analyze cash flow and make sure cash will be available to pay taxes when they fall due, but don't put money aside for this in Treasury bills or commercial paper at 4% to 6%. Put that money in the business at 10%, 15%, or 25%."

CORPORATE TAX ACCELERATION

There have been two recent rounds of acceleration of corporate income taxes. I shall examine them in chronological order.

JFK round

President Kennedy reduced corporate tax rates, but he stepped up the payment dates. Prior to this, larger corporations paid somewhat under half their income tax in the latter half of the tax year during which the liability arose and paid the greater part in the first half of the following year.

The unilaterally imposed quid pro quo for the cut in rates was a gradual move to a modified pay-as-you-go basis by 1971. This was accomplished by having corporations begin paying their federal income taxes in the quarter in which the liability arose.

This acceleration had varying effects on the corporate taxpayer depending on his size and, more particularly, on his growth rate.

EXHIBIT I.—EFFECTIVE FEDERAL CORPORATE INCOME TAX RATES (CASH TAX RATES)

[In percent]

Year	Zero growth	5 percent growth	10 percent growth	15 percent growth
1963	52.00	50.45	49.05	47.76
1964	52.00	50.45	49.05	47.76
1965	51.38	49.93	48.61	47.44
1966	51.60	50.30	49.13	48.06
1967	51.60	50.48	49.46	48.53
1968	51.60	50.65	49.46	49.00
1969	50.16	49.38	48.68	48.05
1970	50.16	49.49	48.85	48.31
1971	48.00	47.43	46.91	46.43

Effective federal corporate income tax rates under acceleration are shown in *Exhibit I* for various corporate earnings growth rates. (Hereafter, these will be termed "cash tax rates," meaning income taxes *paid* during the year divided by taxable earnings during that year. This measure of the actual tax burden on cash flow is better than pairing tax accruals with current earnings.)

The exhibit shows the combined effect on taxable income of the "reduction" in rates and of the speedup. It should be noted that taxable income as used here is not what a corporation shows in its annual report to shareholders, but what it includes in its tax return.

In making payments on their estimated federal income tax liability, corporations currently do not incur any penalty for underpayment if they pay a minimum of 70% of the actual liability. The exhibit assumes that corporations make payments at a 75% level of actual liability, building in a 5% margin for error (75% is also the figure used by the Council of Economic Advisers for this purpose).

Exhibit I indicates that there has been no reduction in the actual burden of corporate income tax payments as measured against taxable corporate income. The direct tax reduction (the cut in rates) was indirectly repealed for a period of seven years by means of acceleration of payments.

At the same time that acceleration went into effect, however, corporate income taxes were reduced by means of the second phase of the 7% investment credit. The exhibit does not take into consideration the effect of the 7% credit. This is deliberate so as to isolate acceleration and show its unfavorable effects.