

Commerce and Transportation

Investment credit.—Most businesses may take a tax credit equal to 7 percent of the cost of investments in new machinery and equipment made during the year. This credit does not lower the basis of the property for calculating the deduction for depreciation.

Excess depreciation on buildings.—To the extent that allowable depreciation for tax purposes exceeds the rate at which assets actually depreciate, business tax liabilities are deferred. Businesses may employ a variety of depreciation schedules for tax purposes, some of which cause a much larger part of asset values to be written off in early years of the asset's useful life than do others. The revenue cost of allowing for buildings depreciation methods for tax purposes that reduce asset value more rapidly than straight-line depreciation (the method typically used in financial statements) is shown below. The part based on rental housing is listed under community development and housing. The tax depreciation allowed for machinery and equipment is closer to actual depreciation than that allowed on buildings. In addition, the code permits full recapture as ordinary income of profits resulting from excess depreciation on machinery and equipment, but recapture of only a declining and then disappearing proportion of such profits on buildings. In view of this and the difficulty of estimating the divergence, if any, between depreciation allowed for tax purposes and actual depreciation, depreciation for machinery and equipment is not included here as a tax expenditure.

Dividend exclusion.—Individual income taxpayers may exclude \$100 of dividends from income subject to tax.

Capital gains—Corporation income tax.—Capital gains of corporations are subject to a tax of 25 percent while the rate applicable to other corporate income above \$25,000 is 48 percent (excluding the temporary surcharge).

Bad debt reserves of banks and other financial institutions.—Commercial banks, mutual savings banks, building and loan associations, and cooperative banks are permitted to set aside bad debt reserves based on stipulated fractions of deposits, of loans outstanding, or of taxable income before computation for bad debts. The amounts set aside typically greatly exceed actual loss experience and reasonable expectations as to future losses.

Credit unions.—Credit unions are exempt from Federal income tax.

Deduction of interest on consumer credit.—Interest paid on consumer credit is allowed as an itemized nonbusiness deduction for individuals.

Expensing of research and development expenditures.—Expenditures by businesses for research and development (R&D) are carried out to find new products or processes, to reduce costs, or for other purposes. In nearly all cases, benefits from such expenditures will accrue for well over 1 year. For tax purposes business may deduct all R&D expenditures in the year during which they are incurred, or they may amortize them over not less than 5 years.

Surtax exemption (\$25,000).—Corporations pay income tax at the rate of 22 percent on all taxable income plus a surtax of 26 percent on taxable income in excess of \$25,000 (excluding the temporary surcharge). Each corporation therefore enjoys a surtax exemption of \$25,000. This exemption is intended to encourage small or new businesses.

Deferral of tax on shipping companies.—Certain companies which operate U.S. flag vessel on foreign trade routes receive an indefinite deferral of income taxes on that portion of their net income which is used for shipping purposes, primarily construction, modernization, and major repairs of ships.