

WebMemo



Published by The Heritage Foundation

No. 2915
May 26, 2010

Kerry–Lieberman Tax Subsidies: The Wrong Approach for Nuclear Power

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When it comes to tax policy, what once were vices now are habits. A quick glance at the tax provisions in the President's budget reveals lists and lists of special tax deductions and credits. Legislation again moving in Congress to extend certain expired and expiring tax provisions includes yet another list of special tax provisions.¹ Inevitably, the number of special tax breaks scattered throughout the tax code increases until just about every piece of substantive legislation moving through Congress has its own tax title with additional tax subsidies to bestow on the fortunate few.

A classic example of this habitual vice is contained in the Kerry–Lieberman climate bill. This bill, which contains some good provisions on nuclear energy, contains six special tax breaks just for the nuclear power industry.² Few Members of Congress fail to complain about tax complexity and tax expenditures. Apparently, just as few fail to litter the tax code with their own policy candy wrappers. As a start, Congress should recover its long-lost restraint in devising new ways to micromanage the economy through the tax code and use the revenues gained to lower tax rates and make a real, substantive difference for the economy.

An Occasional Treasury Perspective on Tax Subsidies. In its "Reasons for Change" discussion, the U.S. Treasury Green Book describing the President's fiscal year 2011 tax proposals explains that a particular tax credit, like other preferences the Administration proposes to repeal, distorts markets by encouraging more investment in the industry than would occur under a neutral tax system.³ To

the extent the credit encourages overproduction, it is detrimental to long-term energy security.

To be clear, the slightly paraphrased reference in the Green Book is to the oil and gas industry and the President's proposals to eliminate fossil fuel subsidies. These are sound proposals, but the Administration's laudable preference for a neutral tax system is decidedly spotty. For example, at the same time the Administration is proposing to eliminate oil and gas subsidies because they distort the allocation of resources, it proposes to extend and increase an equally distorting tax credit relating to clean energy manufacturing—the Section 48(C) program.

The Kerry–Lieberman climate change bill poses a major threat to the health of the U.S. economy. Yet within that otherwise fatally flawed bill lies a nuclear title that could provide the foundation for good nuclear-only legislation. Among the positive provisions, the nuclear power title brings about important regulatory reform to speed up the permitting process for new plants and consolidates research and development for used fuel recycling under one facility.

Unfortunately, the nuclear power title also includes examples of Congress's tax policy vices. For example, it would:

This paper, in its entirety, can be found at:
<http://report.heritage.org/wm2915>

Produced by the Thomas A. Roe Institute
for Economic Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002-4999
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- Allow five-year accelerated depreciation for new nuclear power plants;
- Allow a 10 percent investment tax credit for nuclear power facilities;
- Include nuclear power facilities in the qualified advanced energy project credit;
- Allow allocation of the credit for production of advanced nuclear power facilities to private partnerships with nuclear power;
- Allow tax-exempt private activity bonds to be used for public–private partnerships for advanced nuclear power facilities; and
- Provide grants for qualified nuclear power facility expenditures in lieu of tax credits.

The issue here is not whether nuclear power should go forward. The issue is the government's bad habit of attempting to pick successful technologies of any sort to favor and others to disfavor. There is nothing wrong with hoping or expecting that one sort of energy or one sort of technology will ultimately prevail in the marketplace. Moreover, if one believes so firmly in the advantages of one energy or technology over another, capital markets allow one to encourage and participate in its success or failure.

Tax provisions like those relating to nuclear power provisions in the Kerry–Lieberman bill do something else entirely. They use the power of the federal purse to artificially influence the development of these markets and technologies. There is no reason to believe Congress has better information or can process that information in this area any better than private market participants investing their own money.

Markets are not perfect. Markets make mistakes. And government has a modest but clear role to play in the process. But on balance and over time, market participants facing price signals undistorted by government policies make fewer and less costly mistakes, and they correct mistakes more quickly.

Private market participants will generally allocate resources so as to produce the most value at the least cost. Every instance in which government decides it knows best is another instance in which policymakers have decided they know better. Government would do more good by not distorting price signals on which private market participants make decisions or favoring certain parties through the tax code.

Infant Industries and International Markets.

Two arguments that may be raised to defend these nuclear power tax subsidies are that they are needed temporarily to get an “infant” stage industry moving forward and that the credit is needed for the U.S. to catch up to other countries in the use and development of nuclear power. Both arguments miss the mark badly.

The U.S. nuclear industry is hardly an infant industry in the traditional sense, yet the decades-long hiatus in new U.S. nuclear power plant construction has left this part of the U.S. industry much less mature than many foreign competitors. Even so, the abiding obvious and traditional problem with the temporary tax credit/infant industry argument remains that the word *temporary* is typically redefined over time to include periods that can last for decades. “Temporary” can take on near cosmological dimensions.

Indeed, the Energy Policy Act of 2005 provided production tax credits, insurance against regulatory delays, and authorized loan guarantees, all of which were justified as being the “temporary” help needed to restart America's nuclear industry. Moreover, nuclear suppliers are already increasing their capacity to meet anticipated market demand, absent additional tax subsidies.

Another problem with tax credit subsidies is that they typically protect industries from economic pressures and thus hinder them from becoming internationally competitive. If these nuclear power

1. See Committee on Finance, U.S. Senate, “The American Jobs and Closing Tax Loopholes Act of 2010,” May 20, 2010, at <http://finance.senate.gov/newsroom/chairman/download/?id=79e24697-02a8-4265-8c56-6f7a00703c36> (May 26, 2010).
2. See “The American Power Act: Section by Section,” at http://lieberman.senate.gov/assets/pdf/APA_sect.pdf (May 25, 2010).
3. See U.S. Department of the Treasury, “General Explanations of the Administration's Fiscal Year 2011 Revenue Proposals,” February 2010, at <http://www.treas.gov/offices/tax-policy/library/greenbk10.pdf> (May 25, 2010).

tax subsidies are enacted, then there is a serious danger that by distorting the marketplace they may condemn the domestic industry to second-class status on the world stage.

The U.S. industry lags its foreign competitors in part due to an anti-nuclear bias that, fortunately, appears to be fading. But the U.S. lag is also due in part to the financial encouragements of foreign governments through their own tax subsidies, direct payments, loan guarantees, and the like. While it is tempting to match these countries foolishness for foolishness, that is not a gap the U.S. should seek to close.

Instead, the U.S. should focus on establishing an efficient regulatory regime for nuclear power that allows the industry to grow on its own merits. These other countries have borne heavy costs in creating subsidies to distort their markets badly so as to gain an advantage. But this advantage will prove temporary—especially when competing against market-competitive U.S. suppliers—as market distortions accrete while their industries become ever-more dependent on these subsidies to survive in the global marketplace.

Stop Micromanaging the Economy. The nuclear power tax provisions contained in the Kerry–Lieberman bill are hardly the most noxious of all such tax subsidies contained in the tax code. They are no less unwise, however, for the very reasons Treasury lays out in its discussion of proposals to repeal similar tax provisions relating to the oil and gas industry: They distort economic activity and diminish economic vitality.

In this case, as in so many, Congress should break the habit of littering the tax code with special exemptions, deductions, credits, exceptions, and exceptions to exceptions that constitute the sum total of past efforts to micromanage the economy through an already inherently complex income tax system. Nuclear power's economic strengths are more than sufficient to re-establish the industry in the U.S. without a new dose of corporate tax welfare.

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