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Business

The tax on publicly listed corporations makes it slightly more costly for companies to repurchase their shares.

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By Laura Davison, Bloomberg News (TNS)

A new tax created by Democrats to slow a record pace of stock buybacks has been largely shrugged off by corporations that see the 1% excise levy as a minor cost of doing business.

The tax on publicly listed corporations—created in President Joe Biden's signature

Democrats had hoped that increasing the cost of stock buybacks would prod companies to use their cash on hand to raise workers' wages or invest in new endeavors, bolstering the economy.

Chances of such an outcome might have been higher if early versions of the tax had come to pass. But proposals for a 2% levy and prohibiting buybacks unless companies met criteria like a minimum $15-an-hour wage didn't materialize.

Corporations lobbied hard against those proposals, and the result was the smaller tax, with none of those strings attached.

"A lot of companies have factored that in," Dave Camp, a former chairman of the House Ways and Means Committee who now advises on tax policy issues at PricewaterhouseCoopers LLP, said of the 1% tax. "It's part of the cost of doing business."

Corporations that conduct large-scale buybacks stand to pay, collectively, a hefty chunk of the $73.7 billion congressional scorekeepers project the tax will generate over a decade.

Buybacks are on track for a record-breaking year—before the new levy, Goldman Sachs Group Inc. had predicted a $1 trillion total. And there's little sign that the tax is proving a decisive factor in curbing appetites.

Since congressional passage of the measure on Aug. 12, 16 companies in the S&P 500 Index have announced buyback plans, according to data compiled by Bloomberg. The list includes Johnson & Johnson, Home Depot Inc. and T-Mobile U.S. Inc.

Instead, rising interest rates have been a constraint, with JPMorgan Chase & Co., Citigroup Inc. and Best Buy Co Inc. pausing some repurchases.

“We aren’t seeing anything that is driven primarily by the tax concern,” said Elena

Rep. Kevin Brady, the top Republican on the House Ways and Means Committee, said members of his party will push to repeal the buyback tax when the GOP regains control of Congress. “At the end of the day this is really a tax on savers and retirees,” he said.

Buybacks became a popular way to increase value for shareholders in part because of favorable tax treatment. When companies pay dividends, stockholders are subject to paying tax on those distributions. But with a buyback, the operation can boost the value of the shares—enhancing shareholders’ wealth—without any taxes owed until the owners decide to sell, when they would owe capital gains.

“For decades, stock buybacks were heavily favored by the tax code, despite their skewed benefits for the very top and potential for insider game-playing,” Senate Financial Services Chairman Ron Wyden, an Oregon Democrat, said in a statement. “Our goal wasn’t to end stock buybacks all together—the stock buyback tax simply tries to reduce this preferential tax treatment in order to level the playing field and encourage more investment in workers.”

Salesforce Inc. is one example of a company doing the opposite of what Wyden had hoped. The cloud-based software maker announced its first-ever buyback of $10 billion this year, and Chief Financial Officer Amy Weaver told investors in September the company plans to allocate between 30% and 40% of free cash flow to buybacks going forward.

The biggest hassle for companies may be the compliance procedures to follow the rules governing the tax, said Scott Levine, a partner at law firm Jones Day.

The Internal Revenue Service has yet to issue any regulations on the buyback tax because it takes time to write those rules, creating a period of uncertainty for corporations.

“Obviously nobody likes a tax increase,” Levine said. “But 1% is not going to be

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