Comments for the Record
U.S. House of Representatives
Committee on Ways and Means
Hearing on Tax Reform and Tax Provisions Affecting State and Local Governments

Tuesday, March 19, 2013, 10:00 AM

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Chairman Camp and Ranking Member Levin, thank you for the opportunity to submit these comments for the record to the Committee on Ways and Means. They are substantially similar to our comments in April of last year to the Senate Finance Committee. Feel free to contact us for a more in depth briefing on our testimony for either members or staff. As always, our comments are in the context of our four part tax reform plan:

- A Value Added Tax (VAT) to fund domestic military spending and domestic discretionary spending with a rate between 10% and 13%, which makes sure very American pays something.
- Personal income surtaxes on joint and widowed filers with net annual incomes of $100,000 and single filers earning $50,000 per year to fund net interest payments, debt retirement and overseas and strategic military spending and other international spending, with graduated rates between 5% and 25% in either 5% or 10% increments. Heirs would also pay taxes on distributions from estates, but not the assets themselves, with distributions from sales to a qualified ESOP continuing to be exempt.
- Employee contributions to Old Age and Survivors Insurance (OASI) with a lower income cap, which allows for lower payment levels to wealthier retirees without making bend points more progressive.
- A VAT-like Net Business Receipts Tax (NBRT), which is essentially a subtraction VAT with additional tax expenditures for family support, health care and the private delivery of governmental services, to fund entitlement spending and replace income tax filing for most people (including people who file without paying), the corporate income tax, business tax filing through individual income taxes and the employer contribution to OASI, all payroll taxes for hospital insurance, disability insurance, unemployment insurance and survivors under age 60.

Our proposals have several impacts on state and local tax and fiscal policy. Those states with fixed conformity provisions regarding income taxation in law or their constitutions will be greatly affected by enactment of a simplified income tax which treats distributions from inheritance as normal income. Indeed, if they do not enact similar reform, which includes a much higher income floor for filing, many more heirs will be touched by this provision than in federal law. As most state income tax rate structures are much less progressive than the federal system, many states will be able to abandon income taxation altogether, possibly increasing use of Land Value Taxes if some form of redistributive tax is still desired.

If the basic structure of reform is adopted in the states, the biggest change will be the need for a common base between federal and state consumption taxes. Shifting from retail sales taxes and gross receipts taxes to value added taxes and VAT-like net business receipts taxes will change the nature of most state taxation, while enabling ease of collection of taxes on online sales, since taxes would be levied at every stage of the production process.

If a common base agreement can be negotiated for these taxes, state treasurers can collect both their own taxes and the federal taxes, as well as analytical information on tax credit usage, which can then be shared with the U.S. Internal Revenue Service in order to track income accruing to payers of the federal high income surtax, as well as to recipients of the federal child tax credit, which would be paid to employees with wages under the NBRT and then verified by a mailing from both the employer and the Internal Revenue Service, with employees verifying that their employees paid every dollar to them reported as a credit.

Our hope is that states would match the Child Tax Credit at a level consistent with their cost of living. Some states might even include higher credits for certain high-cost counties, for instance, Northern Virginia.

The NBRT at both the state and federal levels should fund services to families, including education at all levels, mental health care, disability benefits, Temporary Aid to Needy Families, Supplemental Nutrition Assistance, Medicare and Medicaid. If society acts compassionately to prisoners and shifts from punishment to treatment for mentally ill and addicted offenders, funding for these services would be from the NBRT rather than the VAT.

States may also include several of the educational and social service credits recommended under our proposal. The NBRT could be used to shift governmental spending from public agencies to private providers without any involvement by the government – especially if the several states adopted an identical tax structure. Either employers as donors or workers as recipients could designate that revenues that would otherwise be collected for public schools would instead fund the public or private school of their choice. Private mental health providers could be preferred on the same basis over public mental health institutions. This is a feature that is impossible with the FairTax or a VAT alone.

To extract health care cost savings under the NBRT, allow companies to offer services privately to both employees and retirees in exchange for a substantial tax benefit, provided that services are at least as generous as the current programs. Employers who fund catastrophic care would get an even higher benefit, with the proviso that any care so provided be superior to the care available through Medicaid. Making employers responsible for most costs and for all cost savings allows them to use some market power to get lower rates, but not so much that the free market is destroyed. Increasing Part B and Part D premiums also makes it more likely that an employer-based system will be supported by retirees.

Enacting the NBRT is probably the most promising way to decrease health care costs from their current upward spiral – as employers who would be financially responsible for this care through taxes would have a real incentive to limit spending in a way that individual taxpayers simply do not have the means or incentive to exercise. While not all employers would participate, those who do would dramatically alter the market. In addition, a kind of beneficiary exchange could be established so that participating employers might trade credits for the funding of former employees who retired elsewhere, so that no one must pay unduly for the medical costs of workers who spent the majority of their careers in the service of other employers.

Conceivably, NBRT offsets could exceed revenue. In this case, employers would receive a VAT credit.

There will be no impact on the states of FICA reforms, except to the extent that our suggested reforms yield a higher base benefit for seniors, which will decrease their need for state social service benefits.

Income tax simplification will eliminate the deduction for state income and property taxes. The extent to which state income taxes are eliminated will also eliminate the demand for these, although if states adopt higher land value taxes for redistributive purposes, some residual deduction for this tax may need to be included in the federal tax code, although doing so will simply require higher federal rates to make up the difference. Additionally, abandonment of the state income tax deduction has been seen as a reason to entirely federalize Medicaid as an offset. Doing so may be appropriate, however if participants in subsidized and paid adult education are covered by the provider's insurance as if employees and retirees long term care needs are increasingly covered by the firms they retired from as an offset to Net Business Receipts Taxes, the question of funding Medicaid may be a minor footnote.

Thank you for the opportunity to address the committee. We are, of course, available for direct testimony or to answer questions by members and staff.

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