Comments for the Record
U.S. House of Representatives
Committee on Ways and Means
Hearing on the Treatment of Closely-Held Businesses in the Context of Tax Reform

Wednesday, March 7, 2012, 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 House Ways and Means Committee. Our comments are an expansion of last month's comments and are, as always, in the context of our tax reform plan, which has the following four elements:

- 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.
- 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, personal retirement accounts, 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.

We have no proposals regarding environmental taxes, customs duties, excise taxes and other offsetting expenses, although increasing these taxes would result in a lower VAT. Small and closely held businesses already pay these taxes and will continue to in reform.

Small businesses will pay VAT, although they may not be a VAT collector, depending upon whether business size exemptions are included in any VAT legislation. Their impact would be merely to report the VAT they pay on the receipt so that customers may be aware of taxation while those who use the product in their supply chain can use this information for credits against their VAT collection. Larger businesses which are closely held will pay VAT in the same way public companies do.

Small businesses may likewise not have to pay the NBRT. Indeed, for consultants who work primarily for one client or sell from one supplier, NBRT rules should mandate that small firm employees be treated like employees of the larger firm for purposes of health care coverage and the Child Tax Credit, should the consultant or distributor not meet the income thresholds included for filing. Large business which are closely held will pay the NBRT in the same way public companies do.

Accounting for Employee-paid Old Age and Survivors Insurance will be no more complicated than current law, while accounting for the income surtax will be greatly simplified. Individuals who previously paid their business taxes as part of income taxation will only file the income surtax if they clear $50,000 after paying staff ($100,000 for joint filers and qualified widow(er)s). The only complexity will be accounting for sales to a qualified ESOP, which may continue to be tax exempt – although if personal accounts are enacted under OASI it may be wise to repeal the ESOP deduction so that the wave of ESOP conversions that will result will allow a substantial pay down to the national debt, which will more quickly allow the sunset of the income surtax.

Establishment of personal accounts as an offset for Old Age and Survivors Insurance will require complex accounting rules, but only for firms which pay the NBRT. Again, consultants and distributors who do not should be afforded the opportunity to accumulate personal accounts through the larger firm they deal with, buying their company stock as if they were full-time employees. For example, workers at car dealerships would have the opportunity to invest in personal accounts of that manufacturer, even if the dealership is large enough to pay the NBRT. Larger closely held firms may also wish to rethink their form of ownership to take advantage of the opportunity personal retirement accounts afford for both capital accumulation (for both firms and individuals) and for succession planning.

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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This testimony is not submitted on behalf of any client, person or organization other than the Center itself, which is so far unfunded by any donations.