

SENATE COMMITTEE ON FINANCE
Tax Reform and the Tax Treatment of Debt and Equity
Senator Olympia J. Snowe
July 13, 2011

Chairman Baucus, Chairman Camp, I thank you both for bringing Congress' two tax-writing Committees together for this historic hearing. Not since 1940 have both the Finance and Ways & Means Committees joined together to hold a joint tax hearing and I am proud to be a part of this momentous occasion.

I also wish to commend you for highlighting the critical issue of the treatment of debt and equity in our tax code as the subject for today's hearing, and also for asking the Joint Committee on Taxation to put its considerable resources to the task of analyzing the significant impact this seemingly obscure topic has on the larger economy.

Our tax code does have a built-in bias that favors the accumulation of debt, particularly relative to the use of equity, and I am troubled by the implications of this fact. By providing a tax deduction for the payment of interest on debt, we have sent a signal to the markets and to businesses that we consider interest payments to be a normal cost of doing business. And the markets have responded with their usual efficiency, as businesses turn to debt for financing, incentivized by the tax code to do so. It is not clear that this incentive effect *created* the financial crisis, but it certainly may have *deepened* that crisis. It is our duty to explore that today, and, if necessary, correct it as part of comprehensive tax reform.

We had a hearing back on March 30th on the ways in which our tax code sends such signals, and I am pleased to have the opportunity to examine one such signal in greater specificity today. Certainly, because the taxation of debt and equity has serious consequences for the economy and job creation, it needs to be given careful consideration in the context of tax reform. But I must ask, yet again, when are we going to proceed to undertake the monumental task of actually enacting comprehensive tax reform? We have had half a dozen hearings so far this year devoted to topics such as today's, all under the rubric of "tax reform," and I commend the Chairman for keeping this issue alive, but at some point we have to move beyond identifying issues to doing something about them.

I have been calling for tax reform for years now. In 2009, when we were invited to the White House for a "Fiscal Responsibility Summit," I chose to discuss tax reform; I pressed it then and I have been doing so ever since. I am disappointed that the Obama Administration has not yet given this critical topic its due attention. As we have

learned from our hearings on tax reform to date, presidential leadership was the lifeblood necessary for passage of landmark tax reform 25 years ago, and Congress has before it a very heavy lift in order to fill the void left us by the Administration and to achieve any kind of serious tax reform again.

To the extent the Administration has talked at all about tax reform, which has been little enough, at least Secretary Geithner and others have recognized that the high U.S. corporate tax rate encourages investors to look to other shores and creates a challenge for American businesses trying to compete in the fierce global marketplace. But with roughly 90 percent of all American businesses organized as flow-through entities, we can hardly focus solely on the narrow issue of corporate tax reform. Rather, we need *comprehensive* tax reform, and that means of necessity that individual rates, at which flow-through entities are taxed, must be part of the conversation. On this point I am pleased to add my voice to that of Chairman Camp, who is with us today and who has made this same argument. Like me, he knows that these businesses are our greatest job creators, providing at least two out of three new American jobs, and the uncertainty they face with looming tax increases after 2012, as the Administration proposes, remains perhaps the greatest and most damaging “signal” our tax system can send.

We hear that tax issues, or even some form of larger tax reform itself, may be a part of the eventual bargain on the debt ceiling issue. While I would welcome any improvements such tax changes may bring, I do not believe that we will benefit from rushed deliberations on taxes to cobble together a debt deal. The path to true and effective tax reform may be arduous but we need to walk that path. I also fear that revenue changes that might be well-suited to offsetting needed and beneficial tax code changes could be used to “pay for” part of the debt deal, making the task of comprehensive tax reform that much more difficult.

Mr. Chairman, the process of reforming the tax law in 1986 was largely possible only through bipartisan work in the Senate Finance Committee and only over the course of years. Thus, we need to start that process now, we cannot wait any longer. I appreciate the meaningful contribution today’s analysis of debt and equity taxation will add to the discussion, but I urge us as a Committee to undertake the larger endeavor of comprehensive tax reform with care and deliberate speed. Our economy needs the boost that tax improvements will provide, and our fellow Americans need the jobs that will come with it.