PROPOSAL FOR COMPREHENSIVE TAX REFORM VIA THE BUSINESS TRANSFRER TAX

by
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PROPOSAL FOR COMPREHENSIVE TAX REFORM VIA THE BUSINESS TRANSFER TAX

EXECUTIVE SUMMARY

The U.S. has experienced a profound reversal of the competitiveness of its industrial sector, primarily due to the federal tax code. Double taxation of saving for investment and high marginal income tax rates on domestic producers are serious barriers to sufficient domestic capital formation. But the tax code's most problematic feature is lack of border adjustment. The disadvantages for U.S. producers of border adjusted VATs averaging 18% added on U.S. exports to foreign markets, and 18 percent rebated on foreign imports in U.S. markets are virtually insurmountable, given the rapid diffusion of technology and innovation in world markets.

Single rate taxation on consumption with deferral of taxation on saving for investment until consumed proposed by most tax reform alternatives, must also be joined with border adjustment comparable to foreign VATs in order to arrest the demise of the U.S. manufacturing sector, as well as to provide territoriality to retrieve corporate headquarters and combat outsourcing of business services.

The Business Transfer Tax (The BTT), a subtraction method value added tax is proposed as the most efficient, equitable and growth oriented basis for border adjusted and consumption based taxation, on the broadest base and at the lowest rate. At a 17% rate, the BTT would provide "tax revenue neutral" replacement of the individual and corporate income taxes, employer social insurance taxes, the estate and gift taxes, plus customs duties. The BTT at a "tax burden neutral" rate of 18.2% would replace these taxes, plus based upon the current three quarters of a trillion dollars trade deficit would provide $127 billion "found money" from levy on net imports, first to provide funding for transition costs, then for closing of the federal deficit.

The BTT is the best prospect for accelerating growth of investment and incomes for all Americans as a consequence of closing the trade deficit, the fiscal deficit and the soaring gap, plus restoration of a sound currency.

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THE NECESSITY OF COMPREHENSIVE TAX REFORM

The U.S. has experienced a profound reversal of competitiveness from the world's dominant industrial power to a country that is failing to compete effectively at home or abroad. This reversal is principally due to a federal tax code that is asymmetrical to the border adjusted value added taxation of all our foreign competitors, and that disincentivizes the productive processes of the American economy.

The U.S. manufacturing sector share of GDP has declined over 50 percent, and over 60 percent as a share of employment. Currently the U.S. has a trade deficit in goods with every principal country in every category of good except federal subsidized aircraft. Only $2 worth of every $3 in goods the U.S. consumes is currently domestically produced. A similar trend is developing in the business services sector due to foreign outsourcing, in part due to removal of corporate headquarter abroad.

"Supply side" economists have made a persuasive case for reform of a federal tax code that double taxes saving for investment at progressive marginal rates, and replacing it with proportional consumption taxation and deferral of saving for investment until consumed. But they have left unaddressed foreign replacement of tariffs with border adjusted value added taxation (VATs) of goods not afforded U.S. manufacturers.

Under U.S. leadership since WWII average OECD tariffs declined from 40 percent rates to 4 percent, (1.7 percent for the U.S.). However, starting with Europe all principal U.S. competitors have now replaced tariffs with border adjusted VATs averaging 18 percent. Consequently, U.S. goods carry a full burden of U.S. federal, state, and local taxes, plus an added 18 percent in foreign markets, and face foreign goods enjoying 18 percent VAT rebates in U.S. domestic markets. The U.S. trade deficit and the virtual demise of the U.S. manufacturing will not be resolved satisfactorily without border adjusted – not just consumption based – tax reform. Devaluation has not and will not resolve this crisis as long as the U.S. is willing to exchange its productive assets for foreign trinkets, ("America for Sale"); nor will U.S. productivity and innovation prevail given its rapid diffusion abroad.

TAX REFORM CRITERIA AND ALTERNATIVES

The crisis described clearly established ***border adjustability*** as a, if not the, most important criterion, critical for effective tax reform. Its potential effect upon competitiveness, and reversal of manufacturing and business service sectors from decline to growth make a more urgent political case for tax comprehensive reform. Current contenders as alternatives for tax reform all are comparable in being ***consumption based***, ***deferring taxation of saving*** for investment until consumed, and ***lowering marginal rates*** usually with a single "flat" rate; or, "hybrids" based upon a dual tax reform. The devil, however, lies in the details. Also important is the necessities that reform should ***simplify*** the code, and that any new tax should be in ***replacement*** of not in ***addition*** to current taxes, ***realistically assessable politically***, and justified on a ***revenue neutral*** basis.

Of the five alternatives most seriously proposed for fundamental consumption based tax reform, the "Flat Tax" and the "consumed income tax" are "direct taxes" that cannot be border adjusted under WTO rules. Both the "retail sales tax" and the European-type "credit invoice VAT taxes" are "indirect" and therefore WTO qualified, but both have proven limited in breadth of assessable tax base for political reasons, resulting in unacceptably higher rate and/or lesser revenue yield, limiting capability for comprehensive replacement of undesirable taxes. The "business transfer tax (BTT)" as a "subtraction method VAT" is an indirect tax on consumed income which should be assessable on all commerce and government for the broadest base and the lowest marginal rate, and WTO qualified for border adjustment; as such it is proposed as the best candidate for comprehensive tax reform.

DESCRIPTION OF THE PROPOSAL

It is proposed that three-quarters of the federal tax code be fundamentally reformed by ***replacing corporate and individual income and related federal taxes with an indirect consumption based and border adjusted Business Transfer Tax (the BTT).***

The tax base for the BTT would be a levy upon all commercial activity and governments determined as follows:

BTT TAX BASE

Commercial:	All Revenues (Excluding Export Sales)
less:	All Purchases of Goods and Services
	(Including Equipment and Structures, but Excluding Imports)
less:	All Charitable Qualifying Donations
Governmental:	All Employment Expenses
	All Imported Goods and Services

As such the BTT is a consumption tax which is levied upon value added after exemption of investment, which is border adjusted by exclusion of exports and inclusion of imports. All commercial activity is proposed for inclusion whether by corporations, partnerships, individuals, or non-profits. Governments are included by levy on employment and the inclusion of BTT in their consumption expenditures at the commercial level. The BTT based is estimated at the macro level as final sales of GDP, less gross commercial private investment and private philanthropic giving (see EXHIBIT I-A attached).

The proposed BTT receipts were determined as the total necessary to fully replace the following present federal taxes:

BTT FEDERAL TAXES TO REPLACE

Individual Income Taxes

Corporate Income Taxes

OASI, DI and HI Employer Taxes

Estate and Gift Taxes

Customs Duties and Fees

Replacement of these taxes was estimated as tax revenue neutral for FY 2003 federal taxation (see EXHIBIT I-B). Also included was provision for rebates of BTT on family based poverty level income totaling $1.5 billion (EXHIBIT I-C). After transition serious consideration should be given to conversion of rebates to vouchers for deposit to universal medical savings accounts.

The BTT tax rate estimated on this basis is a single rate 17 percent as shown in EXHIBIT I-D.* The 17 percent BTT is *tax revenue neutral*, but is a lesser burden to U.S. taxpayers due to *border adjustability adding net foreign imports to the tax base. At one half of a trillion dollars the FY 2003 current trade deficit taxed at 17 percent BTT provided 87 billion per year "found money" as lesser burden for U.S. taxpayers. If the BTT were levied at an 18.2 percent ***tax burden neutral rate***, at the current three quarter of a trillion dollars current trade deficit it would provide $127 billion "found dollars" for federal deficit reduction.

OTHER ISSUES

Provision for ***equitable transition*** could be provided by a reasonable transition to the BTT over a three year period by levying the BTT in one-third increments, while phasing out the present code in one-third increments. Undepreciated assets could be accelerated over a ten year period at the BTT rate. A phase-in of the BTT would result in less of a shock to foreign producers and allow replacement of manufacturing capacity to minimize inflationary pressures.

The ***distribution*** of the BTT relative to lower and middle incomes is comparable to the present tax code's standard deduction, exemptions, and credits in total, given proposed replacement of employer social insurance taxes (generally considered effectively incident upon employees), plus rebates on poverty level incomes. It is intended that it be legislated that an annual amount of money be transferred to the OASI, DI, and HI trusts equal to individual FICA and Medicare taxes as from current employer taxes; as assessed, this effectively eliminates the so-called "bubble", since the individual portion is self-serving. Whether a single rate BTT is effectively less progressive than present individual personal and business taxation is a complex question of effective incidence. There is persuasive evidence that the ultimate burden of progressive and multilayered taxation of physical and even intellectual capital does not really redistribute income. An intended consequence of this proposal is to return to a tax code where all citizens are taxed proportionate to what they consume, except for the bare necessities, comprising the most ***equitable*** basis, and the basis for optimal growth of all incomes.

Exemption of ***charitable giving*** would be provided for all commercial sources of income by the definition of the tax base, which would allow deduction. Wage and salary earners and other non-commercial sources would be allowed to file for rebates on their charitable donations.

The treatment of ***home ownership*** would be much the same as under the present tax code, in that cost of home building includes income taxes at present which would be replaced by the BTT, and since home purchases are not expensed, home resales would not be taxed, nor would home rentals be expensed as at present. Home mortgage interest would not be tax deductible, but would receive the offsetting benefit of lower interest rates due to greater supply of saving for investment. Current home owners' mortgage interest deduction should be considered for transition cost rebates for as long as current rates remain fixed.

Determination of BTT obligation and collection should be via tax returns which would use data already collected for income taxes and be far ***simpler returns***. The importers and exporters would typically be responsible for paying BTT on imports, and filing for rebate of BTT on exports. The BTT can be rendered as ***transparent*** as a retail sales tax by requiring a statement of BTT rate upon all invoices and receipts. This statement would be considered by the IRS as a legal declaration that any purveyor of goods and services has appropriately filed a BTT tax return. The BTT should be even more ***stable*** than Gross Domestic Product, in that it excludes from the tax base the more volatile Gross Private Commercial Investment account.

The ***border adjustability*** of the BTT at the 17 percent or 18.2 percent rates would have a profound effect upon the U.S. manufacturing sector when combined with the expensing of investment. The current trade deficit in goods at over 6 percent of GDP would return to balance of exports and imports as a consequence of leveling the international trade arena given BTT rates imposed on exports and rebated as privileged to all other OECD competitors at rates from 15 percent to 25 percent, averaging 18 percent. ***Territoriality*** of corporate profit taxation included in the BTT would result in the return of corporate headquarters which went abroad to escape U.S. taxation of foreign earned profits. The lost business services that served these corporate headquarters would

return, and export of business services would be augmented by border adjusted rebates of BTT, and outsourcing diminished due to levies of BTT as imports.

CONCLUSIONS AND RECOMMENDATIONS

The combined effects of border adjustability and consumption based taxation would create far higher saving for investment and more rapid growth of U.S. output and incomes to help close the federal deficit and close the U.S. saving gap. Given the multiplier effect of capital intensive return to a growing manufacturing sector, U.S. economic growth would boom, and the restoration of vigorous growth in blue collar and family incomes would reinforce that boom. Economic growth could be remarkable. Whereas transition to consumption taxation in general could be expected to add perhaps 5 percent to 10 years economic growth, the BTT could result in more than double that amount.

In summary, the border adjusted and consumption based BTT offers the best prospects of any alternative for simple, transparent, equitable, and efficient taxation that ends double taxation of saving for investment, provides a leveling of the foreign trade playing field for U.S. producers and promotion of vigorous growth and stability of output and incomes, plus a return to balanced budgets and a stable currency.

A "hybrid" combination of the BTT with either a retail sales tax or a single rate income tax on upper income individuals could provide less desirable, but workable, alternatives. The retail sales tax is just another tax to collect with the same effects at a higher combined rate. Worse still, retaining the income tax could invite the pressures for future finance of an expanded welfare state. ***What is desirable upon proof of the BTT's virtues would be revoking the sixteenth amendment for a permanent end to income taxation.***

EXHIBIT I

ESTIMATION OF PROPOSED BUSINESS TRANSFER TAX
(Basis: Revenue Neutral FY 2003)

A. *The BTT Tax Base:* (Source: NIPA FY 2003)

Final Sales of Domestic Product		$11005.3 bil	
less: Gross Private Domestic Investment		(1665.8)	
plus: Imports of Goods & Services		1517.0	
less: Exports of Goods & Services		(1020.5)	
plus: Owner Occupied Residential Investments		310.6	
less: Owner Occupied Imputed Rent		(697.0)	
less: Private Philanthropic funding		(240.9)	
BTT Tax Base Gross			$9208.7 bil

B. *Proposed BTT Receipts:* (Source: Historical Tables, FY 2006, OMB, FY 2003)

Individual Income Taxes		$793.7 bil	
Corporate Income Taxes		131.8	
Social Insurance (OASI, DI, HI)	671.0		
Employer Share @ 50%	x.50	335.5	
Estate & Gift Taxes		22.0	
Customs Duties & Fees		19.9	
BTT Proposed Receipts			$1302.9 bil
Memo: Social Insurance, Individual		335.5	
Other Retirement Receipts		8.6	
Unemployment-Insurance		33.4	
Excise Taxes		67.5	
Miscellaneous Receipts		34.5	
Continuing Federal Receipts			$ 479.5 bil
Total Federal Receipts (FY 2003)			$1782.4 bil

C. *Determination of Poverty Level Rebates* (Source: BEA FY 2003)

Poverty Level Family Incomes		
Two persons ≥ 65 =	$11133 \div 2 \times 35.9$ mil =	$ 199.8 bil
Two persons < 65 =	$12384 \div 2 \times 173.3$ mil =	$1073.1 bil
Two children ≤ 19 =	18810	
	(12384)	
	$6426 \div 2 \times 81.2$ mil =	$ 260.9
Poverty Level Income Rebate Base		$1533.8 bil

D. *BTT Rate Proposed*

BTT Proposed Receipts		$1302.9 bil
÷ BTT Base, less Rebate Base	$9208.7 - 1533.8 =$	÷ $7674.9 bil
BTT Proposed Rate		17.0%
Memo: BTT Rebates		
BTT Rebate Base		$1533.8 bil
x BTT Rate		x 17.0%
BTT Rebates Proposed		$ 260.7 bil

From the May 2003 issue of Chronicles:

VIEW

The End of Income Taxes
by David A. Hartman

The tax cuts proposed by President George W. Bush take significant steps toward the reform of a federal tax code that retards growth of the capital stock, productivity, and incomes of all Americans. His plan to eliminate the death tax, increase expensing of investment for small businesses, end double taxation of dividend income, expand "returns exempt" taxation of IRA savings, and lower progressive rates on individual incomes are all welcome contributions toward a more efficient tax code. Yet even if it is enacted, the President's proposal will likely add more obstacles to comprehensive reform of the tax code because, once again, tax reform has been launched in a manner that defies economic and political priorities and realities.

The ultimate priority of federal tax reform is to increase savings for investment. To do so, however, by increasing the magnitude of our sizable federal deficit while failing to reduce spending would largely offset the net benefits of such a plan. It is far more effective to change how we tax—that is, to replace lost revenues with better-designed taxation. Tax neutrality is particularly important since the United States is engaged in a war with as-yet-unknown financial demands. And the incipient burden of the baby boomers' retirement requires greater national savings for investment, not increased federal indebtedness.

Since the private economy is mired in a protracted recession, the current priority should be to address tax reform to those areas where taxation is the chief problem. Remediation of the depression in formation of capital stock, depressed corporate income, the massive trade deficit of our uncompetitive manufacturing sector, and the flight of corporate headquarters overseas—which shrinks the compensatory trade surplus in corporate services—should be the targets of the President's reform efforts, yet his reform proposals only marginally address them.

The principal enemy of tax reform continues to be the spurious claim that tax cuts only benefit the rich. It does not seem to matter that the Kennedy and Reagan tax cuts showed definitively that reducing high marginal individual rates and lowering effective corporate rates stimulates growth of investment, output, and incomes for all Americans.

Though our liberal demagogues have failed to understand this, our OECD competitors have taken the message seriously and have relentlessly cut effective taxation on corporations and investment capital. At one time, the United States had the competitive advantage of the lowest corporate taxation in the world. Now, effective corporate taxation in the United States is close to the world's highest, and the ballooning trade deficit in manufacturing and the flight of U.S. corporations abroad are the direct consequences.

Tax-reform measures must address the political appearances of equity. All principal alternatives seek to alter the tax on either consumed income or consumption, excepting only the "necessities" as the basis for optimum equity, efficiency, and growth. In effect, any of these alternatives tax investment savings only once.

By comparison, the current tax code taxes a dollar when earned and saved or consumed; then, it taxes the returns to a corporate dollar invested (even before profits return the invested dollar); then, it taxes a previously taxed dollar of corporate profit received as a dividend or capital gain; and, finally, it taxes up to 55 percent of the remaining savings upon death. The ultimate goal of such a tax code is to discourage capital formation and productive incentives in favor of equality of incomes and wealth—which only occurs in a primitive society.

There are four principal candidates for tax reform. The first is the consumed-income tax, which taxes all income at the individual level only but defers taxation on savings for investment until consumed. The retail-sales tax taxes only consumption (including residential housing), thereby exempting savings for investment until consumed as well. The value-added tax, which proposes a levy on the difference between revenues and expenditures for goods and services, including capital investment (thereby exempting savings for investment until consumed), amounts to a consumption tax. Finally, the "flat tax" is a consumed income tax that amounts to a value-added tax at the corporate level and a "returns exempt" income tax for individuals, which exempts returns to capital (dividends, interest, and capital gains) in order to avoid double taxation.

The devil, however, is in the details. The consumed-income tax is paid (ideally, at a flat, instead of a progressive, rate) on all individual income, but savings for investment is tax-deferred until consumed. The retail-sales tax is assessed at the point of sale levied on retailers. The value-added tax is assessed upon all commercial and governmental entities. But the "flat tax" is assessed as a value-added tax on commerce, and the same flat rate on individual income taxes wages and salaries but does not tax dividends, interest, and capital gains. This is, in fact, tax symmetrical, but it is far too easy to call it an "unfair exemption of the rich."

In the early stages of the tax-reform movement, the "flat tax" designed by Professors Hall and Rabushka was favored by conservative and libertarian economists, probably because it was adopted by Republican House Majority Leader Dick Armey. The "Armey flat tax," however, never gained momentum. Under the direction of Grover Norquist, Americans for Tax Reform has enlisted five "caucuses" in the House of Representatives to promote "zero capital gains tax"; "end the death tax"; "abolish the alternative minimum tax"; "expense capital investment"; and "unlimited IRAs," as steps toward the flat tax. Curiously enough, a caucus to "end double taxation of dividends," the largest of the presently proposed tax cuts, was not created, nor was an "exempt interest" caucus.

The problem with the Armey flat tax, (as Steve Forbes' abortive run for the Republican presidential nomination in 1996 demonstrated) is that a code that proposes to tax Joe Lunchbucket's wages and Sally Steno's salary but not dividends, interest, and capital gains is a sitting duck for class warfare, whether or not it is a well-designed, efficient, and equitable substitute for the present inefficient and inequitable tax code. Both the flat tax and expansion of Roth IRAs (returns-exempt savings) pose the same problem.

Moreover, there is no apparent strategy to implement a stepwise reform of taxation that is tax neutral and, thus, able to avoid the increased deficits that will be produced by the Bush tax cuts. Thus, the new tax-reform movement is heading down a dead-end road. There is little evidence that the public will endorse a revolutionary all-or-nothing reform of federal taxation, financed by escalated deficits.

Our tax-reform gurus are trying to feed the wrong end of the horse. The corporate income tax is double taxation on corporate income. Consequently, the best way to accomplish reform is to replace the corporate income tax with a consumption tax, and the best candidate is a subtraction-method value-added tax. The value-added tax has the broadest tax base, resulting in the lowest rate for a given yield. Since it is territorial (it does not tax foreign income), it would make the United States the preferred location for international headquarters. By exempting exports and including imports, it would help close the trade deficit, since all other OECD competitors have value-added taxes. And by exempting capital investment, it exempts savings for investment, directly promoting the necessary growth of investment for increased productivity and incomes in general, and at the corporate level in particular. Best yet, replacing the corporate income tax with a value-added tax can accomplish this on a tax-neutral basis, without large deficits.

Many conservative and libertarian economists oppose a value-added tax on the grounds that, in Europe, it led to a runaway expansion of government. However, that was the result of imposing the value-added tax in addition to the corporate income tax instead of replacing the corporate income tax. Those who favor a consumption tax such as the VAT claim that the retail-sales tax is preferable, because it is visible. But the VAT can be legislated to be visible and results in lower rates than a retail-sales tax because of its broader base, since the value-added tax will include taxation of government, whereas a retail-sales tax will not.

A ten-percent value-added tax in the form of a business transfer tax that credits payroll taxes (replacing the 35-percent corporate income tax) would provide a sufficient surplus of revenues to convert the personal income tax to a 15-percent single rate. It could further provide the surplus necessary to eliminate all of the principal discriminatory features of the tax code as well—the "death tax," the alternative minimum tax, phaseouts of exemptions and deductions, the marriage and married parenthood penalties, and customs duties. The surplus could also be augmented by converting the earned-income credit to healthcare vouchers, providing relief for Medicaid spending. It could further convert the 15-percent single-rate tax to a consumed-income tax, allowing unlimited deferral of income tax on saving for investment until consumed. And all of this can be accomplished on a tax-neutral basis without added deficits.

Over the course of a decade, the increased growth of investment, output, and incomes plus broader definition of the consumed-income tax base could allow a ten-percent business-transfer tax and a ten-percent single-rate consumed-income tax. A 20-percent business-transfer tax, however, would achieve the same tax-neutral results. Who would not prefer to see an end to the IRS snooping into his income and assets as a result of ending the corporate and individual income taxes?

David A. Hartman, a retired banker, is chairman of the board of directors of The Rockford Institute.

BACK TO THE MAY 2003 ISSUE

Tax Reform: One Positive Step at a Time
by Stephen Moore and David A Hartman

Treasury Secretary Paul O'Neil recently announced that the highest economic priority for the White House over the next two years will be a wholesale repair of the federal income tax system. Bravo! This is the single most important public policy change that the Bush Administration could make to propel faster long term economic growth for America

The Chairman of the economics Department at Harvard has projected that a move toward a consumption based tax system in America would accelerate economic growth by 1 to 2 percentage points per year. That would be a very big deal over 10 to 20 years. Even a 1% boost in economic growth rates would mean about a 30% higher rise in living standards for middle class Americans. It would also mean a $2 trillion less debt incurred by the government to pay its bills.

At repeated intervals during the past two decades it appeared that the proponents of fundamental tax reform, reinforced by the successful reinvigoration of the United States economy consequent to the Reagan tax cuts, would succeed in "sunsetting" the IRS code and replacing it with a more rational tax on what people take out of the economy (consumption) rather than what they put into the economy (work, risk taking, saving, and investment) But the political process in Washington continues to frustratingly slam the brakes on the reform effort.

In fact, the tax code today is far more progressive, has far higher marginal rates, and is far more inequitably convoluted than after the Reagan cuts A decade long boom driven by historically remarkable technology based productivity improvement has ended, and the United States economy that prospered despite the increased burden of an inefficient federal tax code is now mired in a stubborn recession largely due to that tax burden

The case for tax reform has been made repeatedly in an unimpeachable way for years now Suffice it to say that if we can simplify the code and end the multiple taxation of saving and investment, the benefits will include:

- Substantially faster economic growth
- Less national resources by businesses and individuals wasted on tax compliance
- A less intrusive IRS
- True tax fairness, where the marriage penalty, the death tax, and other inequitable taxes would be eliminated entirely
- Visibility in taxes so that every person knows exactly how much they are paying for the government services we receive—i.e. no more "hidden taxes"

As both the Kennedy and Reagan tax cuts demonstrated, serious reduction of the high marginal rates caused by selective multiple taxation of incomes and capital at high progressive rates, particularly those levied on the corporate sector, will accelerate growth of savings, investment, output and incomes – *all* incomes.

We would add that the United States is under severe pressure to tax more efficiently, given the competitive nature of the open world economy. If the United States has forgotten the lessons of the Reagan tax cuts, the rest of the world has not. Relentless reductions of rates, duplications and effective burden of taxation on foreign corporations have resulted in transition of the United States from one of the relatively lowest to one of the highest corporate tax cost nations.

So how do we get to the promised land? What is the "roadmap to tax reform?" We've been thinking long and hard on this subject (with the beneficial input of some of the smartest minds around the nation, including people like Grover Norquist, Steve Entin, and Jack Kemp) We are convinced that there are a series of incremental steps to tax reform that will pave the road to full income tax elimination. Mr. Norquist calls this approach the "five easy pieces to tax reform, to which we have added what he assumes, that all households must be protected from taxation on necessities.

The following are the proposed principal incremental steps required to fundamentally transform the IRS code to a fair, simple and economically productive consumption tax system:

- REPLACE THE CORPORATE INCOME TAX WITH A "BUSINESS TRANSFER TAX"
- DEFER TAXATION ON INDIVIDUAL SAVINGS UNTIL CONSUMED
- ELIMINATE DISCRIMINATORY TAXATION AND TAX PREFERENCE LOOPHOLES
- FLATTEN TAX RATES SO THAT ALL PAY THE SAME RATE OF TAX
- END THE CAPITAL GAINS TAX, THE DEATH TAX, AND THE ALTERNATIVE MINIMUM TAX
- REBATE FEDERAL TAXES ON NECESSITIES

The proposals presented provide an incremental "pay as you go" fundamental reform resulting in a code comprised of two taxes: a 10 percent "business transfer tax" which is a flat tax on "discretionary consumption", and a 10 percent flat tax on "discretionary consumed income". All other federal taxes other than the individual FICA taxes would be replaced, including the "death tax".

This federal tax code proposal borrows the best of all the other proposals we have seen, including the Armey flat tax and the Billy Tauzin sales tax. The plan also shares many of the same features of the FAIR TAX proposal, which would eliminate the corporate income tax, the personal income tax, and the payroll tax and replace all of this with a national consumption tax.

By jump starting economic growth, the plan would raise more revenues than it loses due to the lower rates and the abolition of unfair taxes. For those who doubt this, we would point to the recent experience with Russia. Russia, under Chairman Putin, recently enacted a 13% flat tax to replace a Byzantine tax system similar to ours in America. Now Russia gets more revenues from the flat tax than it did under the old system with tax rates of 50% or more. And Russia has had a very rapid economic expansion since the new plan was adopted.

We believe that a plan like the one we have proposed could be implemented with a combined tax rate of no more than 20%. The lowest income Americans could be immune from the tax. The resultant composite marginal tax rates on "discretionary consumption" – consumption, excepting necessities – of 20% or so would compare with our current tax system that taxes at a rate of up to 75 percent to invest for and receive a dividend, 60% on capital gains, and 89 percent to invest for an inherited dividend.

Under our plan, no longer will it be necessary to seek economic growth by manipulation of the tax code, social engineering by complex "gives" and "takes" and social equity sought from steeply progressive marginal rates that discourage commerce. An optimal tax code that encourages investment of labor and capital, and taxes only proportionate to that which one takes from the economy, excepting only necessities, will provide an optimum balance of fairness, and an optimum basis for growth of prosperity for all Americans. The only losers would the accountants, tax attorney, and the legions of Washington lobbyists who make their money off of our dysfunctional taxing system What's not to like?

Stephen Moore is a senior fellow in economics at the Cato Institute. David Hartman is Chairman, The Lone Star Foundation, a public policy "think tank" in Austin, Texas. Both are contributing authors to, and Mr. Hartman the editor, of the Institute for Policy Innovation's "Road Map to Tax Reform" project.

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THE NECESSITY OF COMPREHENSIVE TAX REFORM

The U.S. has experienced a profound reversal of competitiveness from the world's dominant industrial power to a country that is failing to compete effectively at home or abroad. This reversal is principally due to a federal tax code that is asymmetrical to the border adjusted value added taxation of all our foreign competitors, and that disincentivizes the productive processes of the American economy.

The U.S. manufacturing sector share of GDP has declined over 50 percent, and over 60 percent as a share of employment. Currently the U.S. has a trade deficit in goods with every principal country in every category of good except federal subsidized aircraft. Only $2 worth of every $3 in goods the U.S. consumes is currently domestically produced. A similar trend is developing in the business services sector due to foreign outsourcing, in part due to removal of corporate headquarter abroad.

"Supply side" economists have made a persuasive case for reform of a federal tax code that double taxes saving for investment at progressive marginal rates, and replacing it with proportional consumption taxation and deferral of saving for investment until consumed. But they have left unaddressed foreign replacement of tariffs with border adjusted value added taxation (VATs) of goods not afforded U.S. manufacturers.

Under U.S. leadership since WWII average OECD tariffs declined from 40 percent rates to 4 percent, (1.7 percent for the U.S.). However, starting with Europe all principal U.S. competitors have now replaced tariffs with border adjusted VATs averaging 18 percent. Consequently, U.S. goods carry a full burden of U.S. federal, state, and local taxes, plus an added 18 percent in foreign markets, and face foreign goods enjoying 18 percent VAT rebates in U.S. domestic markets. The U.S. trade deficit and the virtual demise of the U.S. manufacturing will not be resolved satisfactorily without border adjusted – not just consumption based – tax reform. Devaluation has not and will not resolve this crisis as long as the U.S. is willing to exchange its productive assets for foreign trinkets, ("America for Sale"); nor will U.S. productivity and innovation prevail given its rapid diffusion abroad.

TAX REFORM CRITERIA AND ALTERNATIVES

The crisis described clearly established ***border adjustability*** as a, if not the, most important criterion, critical for effective tax reform. Its potential effect upon competitiveness, and reversal of manufacturing and business service sectors from decline to growth make a more urgent political case for tax comprehensive reform. Current contenders as alternatives for tax reform all are comparable in being ***consumption based***, ***deferring taxation of saving*** for investment until consumed, and ***lowering marginal rates*** usually with a single "flat" rate; or, "hybrids" based upon a dual tax reform. The devil, however, lies in the details. Also important is the necessities that reform should ***simplify*** the code, and that any new tax should be in ***replacement*** of not in ***addition*** to current taxes, ***realistically assessable politically***, and justified on a ***revenue neutral*** basis.

Of the five alternatives most seriously proposed for fundamental consumption based tax reform, the "Flat Tax" and the "consumed income tax" are "direct taxes" that cannot be border adjusted under WTO rules. Both the "retail sales tax" and the European-type "credit invoice VAT taxes" are "indirect" and therefore WTO qualified, but both have proven limited in breadth of assessable tax base for political reasons, resulting in unacceptably higher rate and/or lesser revenue yield, limiting capability for comprehensive replacement of undesirable taxes. The "business transfer tax (BTT)" as a "subtraction method VAT" is an indirect tax on consumed income which should be assessable on all commerce and government for the broadest base and the lowest marginal rate, and WTO qualified for border adjustment; as such it is proposed as the best candidate for comprehensive tax reform.

DESCRIPTION OF THE PROPOSAL

It is proposed that three-quarters of the federal tax code be fundamentally reformed by ***replacing corporate and individual income and related federal taxes with an indirect consumption based and border adjusted Business Transfer Tax (the BTT).***

The tax base for the BTT would be a levy upon all commercial activity and governments determined as follows:

BTT TAX BASE

Commercial: All Revenues (Excluding Export Sales)

less: All Purchases of Goods and Services

(Including Equipment and Structures, but Excluding Imports)

less: All Charitable Qualifying Donations

Governmental: All Employment Expenses

All Imported Goods and Services

As such the BTT is a consumption tax which is levied upon value added after exemption of investment, which is border adjusted by exclusion of exports and inclusion of imports. All commercial activity is proposed for inclusion whether by corporations, partnerships, individuals, or non-profits. Governments are included by levy on employment and the inclusion of BTT in their consumption expenditures at the commercial level. The BTT based is estimated at the macro level as final sales of GDP, less gross commercial private investment and private philanthropic giving (see EXHIBIT I-A attached).

The proposed BTT receipts were determined as the total necessary to fully replace the following present federal taxes:

BTT FEDERAL TAXES TO REPLACE

Individual Income Taxes

Corporate Income Taxes

OASI, DI and HI Employer Taxes

Estate and Gift Taxes

Customs Duties and Fees

Replacement of these taxes was estimated as tax revenue neutral for FY 2003 federal taxation (see EXHIBIT I-B). Also included was provision for rebates of BTT on family based poverty level income totaling $1.5 billion (EXHIBIT I-C). After transition serious consideration should be given to conversion of rebates to vouchers for deposit to universal medical savings accounts.

The BTT tax rate estimated on this basis is a single rate 17 percent as shown in EXHIBIT I-D. **The 17 percent BTT is *tax revenue neutral,* but is a lesser burden to U.S. taxpayers due to *border adjustability adding net foreign imports to the tax base.*** At one half of a trillion dollars the FY 2003 current trade deficit taxed at 17 percent BTT provided 87 billion per year "found money" as lesser burden for U.S. taxpayers. If the BTT were levied at an 18.2 percent ***tax burden neutral rate***, at the current three quarter of a trillion dollars current trade deficit it would provide $127 billion "found dollars" for federal deficit reduction.

OTHER ISSUES

Provision for ***equitable transition*** could be provided by a reasonable transition to the BTT over a three year period by levying the BTT in one-third increments, while phasing out the present code in one-third increments. Undepreciated assets could be accelerated over a ten year period at the BTT rate. A phase-in of the BTT would result in less of a shock to foreign producers and allow replacement of manufacturing capacity to minimize inflationary pressures.

The ***distribution*** of the BTT relative to lower and middle incomes is comparable to the present tax code's standard deduction, exemptions, and credits in total; given proposed replacement of employer social insurance taxes (generally considered effectively incident upon employees), plus rebates on poverty level incomes. It is intended that it be legislated that an annual amount of money be transferred to the OASI, DI, and HI trusts equal to individual FICA and Medicare taxes as from current employer taxes; as assessed, this effectively eliminates the so-called "bubble", since the individual portion is self-serving. Whether a single rate BTT is effectively less progressive than present individual personal and business taxation is a complex question of effective incidence. There is persuasive evidence that the ultimate burden of progressive and multilayered taxation of physical and even intellectual capital does not really redistribute income. An intended consequence of this proposal is to return to a tax code where all citizens are taxed proportionate to what they consume, except for the bare necessities, comprising the most ***equitable*** basis, and the basis for optimal growth of all incomes.

Exemption of ***charitable giving*** would be provided for all commercial sources of income by the definition of the tax base, which would allow deduction. Wage and salary earners and other non-commercial sources would be allowed to file for rebates on their charitable donations.

The treatment of ***home ownership*** would be much the same as under the present tax code, in that cost of home building includes income taxes at present which would be replaced by the BTT, and since home purchases are not expensed, home resales would not be taxed, nor would home rentals be expensed as at present. Home mortgage interest would not be tax deductible, but would receive the offsetting benefit of lower interest rates due to greater supply of saving for investment. Current home owners' mortgage interest deduction should be considered for transition cost rebates for as long as current rates remain fixed.

Determination of BTT obligation and collection should be via tax returns which would use data already collected for income taxes and be far ***simpler returns***. The importers and exporters would typically be responsible for paying BTT on imports, and filing for rebate of BTT on exports. The BTT can be rendered as ***transparent*** as a retail sales tax by requiring a statement of BTT rate upon all invoices and receipts. This statement would be considered by the IRS as a legal declaration that any purveyor of goods and services has appropriately filed a BTT tax return. The BTT should be even more ***stable*** than Gross Domestic Product, in that it excludes from the tax base the more volatile Gross Private Commercial Investment account.

The ***border adjustability*** of the BTT at the 17 percent or 18.2 percent rates would have a profound effect upon the U.S. manufacturing sector when combined with the expensing of investment. The current trade deficit in goods at over 6 percent of GDP would return to balance of exports and imports as a consequence of leveling the international trade arena given BTT rates imposed on exports and rebated as privileged to all other OECD competitors at rates from 15 percent to 25 percent, averaging 18 percent. ***Territoriality*** of corporate profit taxation included in the BTT would result in the return of corporate headquarters which went abroad to escape U.S. taxation of foreign earned profits. The lost business services that served these corporate headquarters would return, and export of business services would be augmented by border adjusted rebates of BTT, and outsourcing diminished due to levies of BTT as imports.

CONCLUSIONS AND RECOMMENDATIONS

The combined effects of border adjustability and consumption based taxation would create far higher saving for investment and more rapid growth of U.S. output and incomes to help close the federal deficit and close the U.S. saving gap. Given the multiplier effect of capital intensive return to a growing manufacturing sector, U.S. economic growth would boom, and the restoration of vigorous growth in blue collar and family incomes would reinforce that boom. Economic growth could be remarkable. Whereas transition to consumption taxation in general could be expected to add perhaps 5 percent to 10 years economic growth, the BTT could result in more than double that amount.

In summary, the border adjusted and consumption based BTT offers the best prospects of any alternative for simple, transparent, equitable, and efficient taxation that ends double taxation of saving for investment, provides a leveling of the foreign trade playing field for U.S. producers and promotion of vigorous growth and stability of output and incomes, plus a return to balanced budgets and a stable currency.

A "hybrid" combination of the BTT with either a retail sales tax or a single rate income tax on upper income individuals could provide less desirable, but workable, alternatives. The retail sales tax is just another tax to collect with the same effects at a higher combined rate. Worse still, retaining the income tax could invite the pressures for future finance of an expanded welfare state. ***What is desirable upon proof of the BTT's virtues would be revoking the sixteenth amendment for a permanent end to income taxation.***

EXHIBIT I

ESTIMATION OF PROPOSED BUSINESS TRANSFER TAX
(Basis: Revenue Neutral FY 2003)

A. The BTT Tax Base: (Source: NIPA FY 2003)			
Final Sales of Domestic Product		$11005.3 bil	
less: Gross Private Domestic Investment		(1665.8)	
plus: Imports of Goods & Services		1517.0	
less: Exports of Goods & Services		(1020.5)	
plus: Owner Occupied Residential Investments		310.6	
less: Owner Occupied Imputed Rent		(697.0)	
less: Private Philanthropic funding		(240.9)	
BTT Tax Base Gross			$9208.7 bil
B. Proposed BTT Receipts: (Source: Historical Tables, FY 2006, OMB, FY 2003)			
Individual Income Taxes		$793.7 bil	
Corporate Income Taxes		131.8	
Social Insurance (OASI, DI, HI)	671.0		
Employer Share @ 50%	x.50	335.5	
Estate & Gift Taxes		22.0	
Customs Duties & Fees		19.9	
BTT Proposed Receipts			$1302.9 bil
Memo: Social Insurance, Individual		335.5	
Other Retirement Receipts		8.6	
Unemployment Insurance		33.4	
Excise Taxes		67.5	
Miscellaneous Receipts		34.5	
Continuing Federal Receipts			$ 479.5 bil
Total Federal Receipts (FY 2003)			$1782.4 bil
C. Determination of Poverty Level Rebates (Source: BEA FY 2003)			
Poverty Level Family Incomes			
Two persons ≥ 65 =	11133 ÷ 2 x 35.9 mil =		$ 199.8 bil
Two persons < 65 =	12384 ÷ 2 x 173.3 mil =		$1073.1 bil
Two children ≤ 19 =	18810		
	(12384)		
	6426 ÷ 2 x 81.2 mil =		$ 260.9
Poverty Level Income Rebate Base			$1533.8 bil
D. BTT Rate Proposed			
BTT Proposed Receipts			$1302.9 bil
÷ BTT Base, less Rebate Base	9208.7 – 1533.8 =	÷	$7674.9 bil
BTT Proposed Rate			17.0%
Memo: BTT Rebates			
BTT Rebate Base			$1533.8 bil
x BTT Rate			x 17.0%
BTT Rebates Proposed			$ 260.7 bil

The Urgency of Border-Adjusted Federal Taxation

By David A. Hartman

David A. Hartman, an economist and retired banker, chairs both the Lone Star Foundation, Austin, Texas, and the Rockford Institute, Rockford, Illinois, and is a frequent contributor of articles on economics and public finance to their respective publications. He recently served as editor and a contributing author for the Institute for Policy Innovation's "Road Map to Tax Reform" project. His special report, "The Strategic Steps to Tax Reform" appeared in *Tax Notes*, Mar. 31, 2003, p. 2033.

In this article, Hartman writes that the urgency of adopting border-adjusted supply-side reform of federal taxation as proposed in "Strategic Steps to Tax Reform" has been made evident by the crisis in the manufacturing sector. That crisis, he says, has been primarily caused by *every* OECD country, *except* the United States, employing border-adjusted taxation in the form of value added consumption taxes on manufactured goods that are rebated on exports and levied on imports at an average rate of 17.7 percent ad valorem. Those VATs, Hartman argues, are a sufficiently insurmountable barrier to U.S. competitiveness to be the primary cause of the negative U.S. balance of trade deficit in manufactured goods with every other major country. The consequences he sees have been a precipitous decline in manufacturing as a share of U.S. value added and employment, a declining "blue-collar labor" share of national income, and transition of the United States from the world's largest creditor to the world's largest debtor, which in turn threatens future U.S. prosperity and security. Hartman exposes what he calls the naivete of those who claim that the seriousness of the problems is imagined or that the crisis will be self-remediating.

The border-adjusted tax reform Hartman proposes would, he argues, be best achieved via the business transfer tax, a subtraction-method VAT that credits employer FICA, exempts investment and exports, and taxes imports. Hartman's first step toward reform would create a 5.5 percent BTT that would replace the corporate income tax and credit employer FICA. The second step would increase the BTT to 10 percent, allowing the imposition of a single 14 percent consumed income tax and elimination of all discriminatory elements of the federal tax code. In the final step, the BTT would be increased to 20 percent and replace the entire federal tax code other than individual FICA, with rebates to all taxpayers of the equivalent of BTT on poverty-level income.

The border-adjusted tax reform proposed in this article, Hartman concludes, would meet the goals of supply-side federal tax reform: It would be neutral, transparent, and impose a single rate of taxation on consumption at the lowest possible marginal rate. But at least as important, he says, is that tax reform using the border-adjusted BTT would level the playing field for U.S. manufacturing and therefore help to close the trade deficit, increase labor incomes, and restore long-term prospects for U.S. competitiveness, prosperity, and security.

Crisis in U.S. Manufacturing

Despite the deep plunge in the stock market, the recent U.S. recession was the shortest and mildest of the post-WWII period when judged by the effect on total U.S. employment. From the peak in July 1998 to the low in January 1999, just six months later, employment declined by only 1.43 million workers. By May 2004, 7.5 million additional people were employed.[1]

But for the U.S. manufacturing sector the employment recession has been the longest and most severe since the Great Depression. Employment in manufacturing jobs fell 3.5 million workers, 19.7 percent of peak payroll in June 1998. As of May 2004, only 187,000 were re-employed, just 1 out of every 19 laid-off employees.[2]

Manufacturing's dollar share of the U.S. economy has been in a relentless decline to less than 50 percent of what its share of Gross Domestic Product was in the 1950s and employment

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[1]*Employment Level (Unadj.)*, Series ID: LN 002000000, U.S. Department of Labor, http://www.bls.gov, July 2004.

Total U.S. Employment Level, Thousands

July 1998	132,769 (peak)
January 1999	131,339 (trough)
Decrease	1,430 (7/98 to 1/99)
May 2004	138,867 (most current)
Increase	7,528 (1/99 to 5/04)

[2]*Manufacturing: All Employees (Unadj.)*, Series ID CEU3000000001, U.S. Department of Labor, http://www.bls.gov, July 2004.

(Footnote continued on next page.)

Briefing Outline:
THE URGENCY OF BORDER ADJUSTED FEDERAL TAX REFORM

A. *The U.S. manufacturing sector is in critical decline due to inability to compete with foreign manufactured goods.*

1. U.S. manufacturing's share of GDP has fallen over 50 percent since the Fifties, and this decline has accelerated to less than 13 percent of GDP since 1998 (EXHIBIT I).
2. Employment in manufacturing as a share of U.S. employment has fallen over 60 percent over the same period, with a 20 percent decline just from 1998, the worst layoff since the Great Depression (EXHIBIT I).
3. The U.S. has a growing trade deficit in goods with every principal country and in every category of goods except government subsidized aircraft (EXHIBIT II).
4. The result has been a "production gap" in manufactured goods which is over 6 percent of GDP; the U.S. now produces only $2 of every $3 of manufactured goods which it consumes (EXHIBIT III).
5. The trade deficit in goods increased to three quarter of a trillion by year end 2004, and the cumulative deficit from 1982 to present has converted the U.S. from the world's largest creditor to the world's largest debtor.
6. The National Association of Manufacturers (NAM) warned last year that "the country may be dropping below critical mass in manufacturing."

B. *A similar trend to manufacturing is developing in the business services sector due to foreign outsourcing.*

1. Growth of the positive trade balance in business services has reversed to a declining trend (EXHIBIT IV).
2. Relocation of corporate headquarters of multinational corporations to secure territorial taxation of income is adding to the loss of U.S. business services abroad.
3. Outsourcing is rapidly expanding in both professional and unskilled white collar services, with an estimated 14 million jobs at risk.

C. *The U.S. manufacturing crisis began soon after foreign replacement of tariffs with border adjusted value added taxation of goods not afforded U.S. manufacturers under the federal tax code.*

1. Under U.S. international leadership, average tariffs of OECD members declined from 40 percent after WWII to 4 percent on average at present; U.S. tariffs now average only 1.7 percent of imports' value.
2. However, starting with France in the mid-Sixties, Europe adopted border adjusted value added taxes now averaging 19 percent, and all OECD competitors other than the U.S. have adopted VATs or equivalents averaging 18 percent (EXHIBIT V).
3. Consequently, U.S. goods carry a full burden of federal, state, and local taxes plus an added average of 18 percent VAT in foreign markets, and face foreign goods which are subsidized by 18 percent VAT rebates in the U.S. domestic market (EXHIBIT VI).
4. The relentless growth in the manufactured goods trade deficit coincides with the successive conversions of foreign competitors to border adjusted taxation, which in effect replaced tariffs (EXHIBIT VII).

D. *The U.S. trade deficit has also been driven by relative reduction and territoriality of foreign corporate income taxes, plus decreased U.S. saving and excessive federal fiscal deficits.*

1. The U.S. now ranks among the highest effective corporate income tax rates in the OECD, and is singular in imposing its domestic corporate taxation rates on foreign income, adding to the manufacturing tax burden.

2. There is a parallel tendency for excessive U.S. federal fiscal deficits to be financed by trade deficits, while tax subsidized foreign goods both incentivize and finance excessive U.S. consumption expenditures.

E. *The U.S. trade deficit will not be resolved with acceptable national consequences without border adjusted and consumption based federal tax reform.*

1. Foreign competitors enjoying an average 18 percent price advantage due to VAT taxation; the joint economies of scale of their domestic markets combined with their now established positions in the U.S., the world's largest market; and often much lower labor costs, will continue to be formidable (EXHIBIT VII).
2. Devaluation of the dollar will not impair competitiveness of foreign competitors until it far exceeds 18 percent, while foreigners will continue to have an appetite for reinvesting trade surpluses in prime U.S. assets. Devaluation will continue to be frustrated by offsetting excessive increase of U.S. prices of capital assets and commodities, and the Fed will continue to limit the extent of devaluation due to unfavorable effects on domestic inflation, plus the role of the dollar as a store of value and as a standard for international exchange.
3. No realistic forecasts show that consumption based federal tax reform *without* border adjustability would come close to remediating an 18 percent price advantage for foreign goods.
4. U.S. productivity gains and innovation will not level the playing field given the rapid diffusion of U.S. technology and management to foreign competitors.
5. The transfer of manufacturing abroad by U.S. companies to secure foreign tax advantages has joined foreign competitors in seriously undermining remaining U.S. competitors.
6. The U.S. Department of Commerce and NAM agendas for restoring competitiveness of U.S. manufacturers if fully achieved would only offset *one quarter* of the typical foreign manufacturing advantage due to border adjusted VAT taxation.
7. In order to level the taxation "playing field" in international commerce, a 15 percent consumption tax adopted on a tax revenue neutral basis is the minimum requirement.

F. *The "Business Transfer Tax" is the most efficient and effective basis for restoring U.S. competitiveness in manufacturing and business services via border adjusted, consumption based federal tax reform.*

1. Of the five alternatives for fundamental consumption based tax reform, the "Flat Tax" and the "consumed income tax" are "direct taxes" not WTO recognizable for border adjustment.
2. Both the "retail sales tax" and the European-type "credit invoice VAT taxes" are "indirect" and therefore WTO qualified, but have proven limited in assessable tax base, resulting in higher rate and/or lesser revenue yield.
3. The "business transfer tax (BTT)" as a "subtraction method VAT" is an indirect tax on consumed income which should be assessable on all commerce and government for the broadest base and the lowest marginal rate, and WTO qualified for border adjustment.
4. Based upon FY 2003 federal revenues, the BTT could replace the corporate income tax (while crediting employer social insurance taxes), the personal income tax, the estate and gift taxes, and custom duties at a tax revenue neutral rate of 16.5 percent, including rebates to all taxpayers of poverty level family income to prevent regressivity (EXHIBIT VIII).
5. No other alteration of public policy nor of the federal tax code can effect a comparable prospect for restoration of the U.S. manufacturing and business services sectors, with consequent growth of saving for investment, growth of incomes and preservation of national security than offered by the BTT.
6. In the event the WTO should refuse to recognize the BTT as an "indirect tax" for border adjustment, then the U.S. should return to unilateral trade negotiation border adjusting its BTT and a tariff as necessary comparable to VAT plus tariff level of each individual country.