

COMMENTS ON THE UNITED STATES INCOME TAX CODE

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INCOME TAXES IN THE UNITED STATES

1. **ACCOUNTANTS ADMINISTER.** Tax accountants and lawyers are usually not economists. There is an Army of people out there who make a living off the income tax system. Advocating a simpler system is not in their best interests. They administer the tax laws. Tax accountants are usually intelligent and accurate. Salesmen sell, accountants follow the tax law. Advocating a simpler system is counter-productive.

2. **DEPRECIATION AN ILLUSION.** Depreciation accounts in our modern accounting system do NOT have a procedure for setting up a RESERVE FOR REPLACEMENT EQUIPMENT. Depreciation is a charge which is balanced with debit and credit entries to cash (or payable) and expense to be charged against income. The federal law does NOT require a separate entry for replacing equipment.

Thus, a Salesman depreciating a \$30,000 car over three years gets less than \$10,000 a year in expense deduction. Assuming, after trade-in, \$6,000 a year, and a 35% tax bracket, about \$4,000 comes off the taxes owed on the return. That would amount to \$12,000 cash in three years, plus perhaps \$12,000 in trade. The replacement car will still cost perhaps \$33,000. Loan interest expense could be a partial help.

A tax-credit system that required a separate entry for replacement equipment might look like this:

Debit (set aside) Reserve for Equipment: \$10,000

Credit (take from) Cash: \$10,000 each year

Current accounting standards and the income tax codes do not provide for or require

replacement. Manufacturing plants have deteriorating equipment which allow world competitors to take their place.

3. ACCOUNTING SYSTEMS MARRIED TO TAX CODE. The modern accounting systems were developed over eighty years to answer the needs of the federal and state income tax systems. An Army of Tax Accountants and Lawyers are primarily employed keeping up with the tax codes., not advocate reform. The tax codes stimulated accounting system development.

4. NEED FOR FLAT TAX. Our federal and state income tax systems have been slowly moving toward a flatter tax. The change will come slowly. The standard deduction and exemptions have been raised to the point that itemized deductions often result in higher taxes than the standard deduction. An Army of Tax accountants and lawyers have a lobby against reform. Some years ago, a major metro newspaper ran a test tax return. The same data was given to a number of reputable tax accounts. All came up with differing returns. An Internal Revenue Service agent came up with a more favorable return for the tax payer than public accountants.

5. IGNORANCE NO EXCUSE. Ignorance of the Law is no excuse. If a state income tax handbook gives the wrong instructions, the tax payer will have to pay a penalty. An IRS agent does not bind the state. An IRS agent cannot deliberately or by error bind the state, so the taxpayer can be held to pay the correct amount plus a penalty. It usually is

not worth the expense to fight, win or lose.

6. MINIMUM WAGE SOLUTION. There is a solution to the MINIMUM WAGE.

The solution is a TAX CREDIT of \$8 per hour and a BENEFITS credit of \$2 per hour.

The minimum wage could remain set where it is. The Tax Credits would be optional for the employer if projected profit margins allowed a commitment... What employer would favor paying taxes to the government if they could be paid to employees.

Older people will work just for health benefits. A health insurance package can be worth \$6,000 to \$8,000 per year tax free. Income Tax is paid on salaries. Younger people are interested in higher pay.

Unions should not fight it if the leadership has its heads on straight. It will help the new employee and loosen up some money for higher bracket salaries. Small business should be happy with it, since it would not be required. If business is not good enough, they are not required to raise wages or benefits.

A political party that prefers the Government doling out assistance will not like it. The political party that believes in reducing taxes will not be able to do it. It might get done in a year or two. The difficult is possible.

7. DEDUCTIONS ARE REGRESSIVE. Deductions make the progressive income tax regressive. They were the con-game of the 20th Century, and now the 21st Century.

Expense account deductions are not worth as much as people think they are. The higher the tax bracket, the more they are worth. Those in a 35 percent tax bracket do not

get back the other 65 percent. If the business trip is necessary, than the deduction is a help. The out-of-pocket and cash costs will still be \$65 out of \$100. Those in 25 percent or 15 percent brackets have even less return.

Deductions may have an effect of lowering a return to a lower tax bracket. Otherwise, the effect is regressive, the opposite of what the United States income tax systems are reputed to be. Those getting 35 percent deductions are getting more back than those on lower incomes.

The cost of tickets for a box seat at the metro professional team are only partially paid by a savings on income taxes. The question for the business is whether the box seats serve another purpose. Advertising expense is necessary, but hard to prove beneficial. The deduction eases the pain.

A flatter tax is fairer to everyone.