109TH CONGRESS
1ST SESSION

H. R. 1040

To amend the Internal Revenue Code of 1986 to provide taxpayers a flat tax alternative to the current income tax system.

IN THE HOUSE OF REPRESENTATIVES

March 2, 2005

Mr. Burgess (for himself, Mr. Hall, Mr. Bonilla, Mr. Scott of Georgia, and Mr. McCaul of Texas) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to provide taxpayers a flat tax alternative to the current income tax system.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the “Freedom Flat Tax Act”.

SEC. 2. FREEDOM FLAT TAX.

(a) In General.—Subchapter A of chapter 1 of the Internal Revenue Code of 1986 is amended by inserting after part VII the following new part:
“PART VIII—FREEDOM FLAT TAX

(1) Sec. 60. Irrevocable election to be subject to flat tax.
(2) Sec. 60A. Tax imposed on individuals.
(3) Sec. 60B. Tax imposed on business activities.
(4) Sec. 60C. Tax on noncash compensation provided to employees not engaged in business activity.

“SEC. 60. IRREVOCABLE ELECTION TO BE SUBJECT TO FLAT TAX.

“(a) INDIVIDUAL.—

“(1) IN GENERAL.—Except as provided in paragraph (2), in lieu of the tax imposed by sections 1 (relating to tax imposed) and 55 (relating to alternative minimum tax imposed), under regulations prescribed by the Secretary, an individual may make an irrevocable election to be subject to the tax imposed by this part.

“(2) INNOCENT SPOUSE EXCEPTION.—An individual who has made an election under paragraph (1) and who subsequently obtains relief of liability for tax under section 6015(b) may, not later than 1 year after the date such relief is granted, revoke the election made under paragraph (1).

“(b) PERSON ENGAGED IN BUSINESS ACTIVITY.—In lieu of the tax imposed by sections 11 (relating to tax imposed) and 55 (relating to alternative minimum tax imposed), under regulations prescribed by the Secretary, a person engaged in business activity may make an irrev-
ocable election to be subject to the tax imposed by this part.

“(c) DISALLOWANCE OF CREDITS.—No credit shall be allowed under this chapter for any taxable year to any person with respect to whom an election under subsection (a) or (b) is in effect.

“SEC. 60A. TAX IMPOSED ON INDIVIDUALS.

“(a) In General.—There is hereby imposed on the taxable income of every individual who makes an election to be subject to this part a tax equal to—

“(1) 19 percent of the taxable income of such individual for such taxable year in the case of the first 2 taxable years of the individual beginning with the taxable year for which the election is made, and

“(2) 17 percent of the taxable income of such individual for such taxable year in the case of all taxable years subsequent to the taxable years described in paragraph (1).

“(b) Taxable Income.—For purposes of this part, the term ‘taxable income’ means the excess of—

“(1) the sum of—

“(A) wages (as defined in section 3121(a) without regard to paragraph (1) thereof) which are paid in cash and which are received during
the taxable year for services performed in the
United States,

“(B) retirement distributions which are in-
cludible in gross income for such taxable year,
plus

“(C) amounts received under any law of
the United States or of any State which is in
the nature of unemployment compensation, over
“(2) the standard deduction.

“(c) STANDARD DEDUCTION.—For purposes of this
part—

“(1) IN GENERAL.—The term ‘standard deduc-
tion’ means the sum of—

“(A) the basic standard deduction, plus
“(B) the additional standard deduction.

“(2) BASIC STANDARD DEDUCTION.—For pur-
poses of paragraph (1), the basic standard deduction
is—

“(A) $25,580 in the case of—
“(i) a joint return, or
“(ii) a surviving spouse (as defined in
section 2(a)),
“(B) $16,330 in the case of a head of
household (as defined in section 2(b)), and
“(C) $12,790 in the case of an individual—

“(i) who is not married and who is not a surviving spouse or head of household, or

“(ii) who is a married individual filing a separate return.

“(3) ADDITIONAL STANDARD DEDUCTION.—For purposes of paragraph (1), the additional standard deduction is $5,510 for each dependent (as defined in section 152) who is described in section 151(c)(1) for the taxable year and who is not required to file a return for such taxable year.

“(d) RETIREMENT DISTRIBUTIONS.—For purposes of this section, the term ‘retirement distribution’ means any distribution from—

“(1) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

“(2) an annuity plan described in section 403(a),

“(3) an annuity contract described in section 403(b),

“(4) an individual retirement account described in section 408(a),
“(5) an individual retirement annuity described in section 408(b),
“(6) an eligible deferred compensation plan (as defined in section 457),
“(7) a governmental plan (as defined in section 414(d)), or
“(8) a trust described in section 501(e)(18).

Such term includes any plan, contract, account, annuity, or trust which, at any time, has been determined by the Secretary to be such a plan, contract, account, annuity, or trust.

“(e) Income of Certain Children.—For purposes of this part—

“(1) an individual’s taxable income shall include the taxable income of each dependent child of such individual who has not attained age 14 as of the close of such taxable year, and

“(2) such dependent child shall have no liability for tax imposed by this section with respect to such income and shall not be required to file a return for such taxable year.

“(f) Inflation Adjustment.—

“(1) In general.—In the case of any taxable year beginning in a calendar year after 2006, each dollar amount contained in subsection (e) shall be
increased by an amount determined by the Secretary to be equal to—

“(A) such dollar amount, multiplied by

“(B) the cost-of-living adjustment for such calendar year.

“(2) COST-OF-LIVING ADJUSTMENT.—For purposes of paragraph (1), the cost-of-living adjustment for any calendar year is the percentage (if any) by which—

“(A) the CPI for the preceding calendar year, exceeds

“(B) the CPI for the calendar year 2005.

“(3) CPI FOR ANY CALENDAR YEAR.—For purposes of paragraph (2), the CPI for any calendar year is the average of the Consumer Price Index as of the close of the 12-month period ending on August 31 of such calendar year.

“(4) CONSUMER PRICE INDEX.—For purposes of paragraph (3), the term ‘Consumer Price Index’ means the last Consumer Price Index for all-urban consumers published by the Department of Labor.

For purposes of the preceding sentence, the revision of the Consumer Price Index which is most consistent with the Consumer Price Index for calendar year 1986 shall be used.
“(5) Rounding.—If any increase determined under paragraph (1) is not a multiple of $10, such increase shall be rounded to the next highest multiple of $10.

“(g) Marital Status.—For purposes of this section, marital status shall be determined under section 7703.

SEC. 60B. TAX IMPOSED ON BUSINESS ACTIVITIES.

“(a) Tax Imposed.—There is hereby imposed on every person engaged in a business activity who makes an election to be taxed under this part a tax equal to—

“(1) 19 percent of the business taxable income of such person for such taxable year in the case of the first 2 taxable years of the individual beginning with the taxable year for which the election is made, and

“(2) 17 percent of the business taxable income of such person for such taxable year in the case of all taxable years subsequent to the taxable years described in paragraph (1).

“(b) Liability for Tax.—The tax imposed by this section shall be paid by the person engaged in the business activity, whether such person is an individual, partnership, corporation, or otherwise.
“(c) BUSINESS TAXABLE INCOME.—For purposes of this section—

“(1) IN GENERAL.—The term ‘business taxable income’ means gross active income reduced by the deductions specified in subsection (d).

“(2) GROSS ACTIVE INCOME.—

“(A) IN GENERAL.—For purposes of paragraph (1), the term ‘gross active income’ means gross receipts from—

“(i) the sale or exchange of property or services in the United States by any person in connection with a business activity, and

“(ii) the export of property or services from the United States in connection with a business activity.

“(B) EXCHANGES.—For purposes of this section, the amount treated as gross receipts from the exchange of property or services is the fair market value of the property or services received, plus any money received.

“(C) COORDINATION WITH SPECIAL RULES FOR FINANCIAL SERVICES, ETC.—Except as provided in subsection (e)—
“(i) the term ‘property’ does not include money or any financial instrument, and

“(ii) the term ‘services’ does not include financial services.

“(3) Exemption from tax for activities of governmental entities and tax-exempt organizations.—For purposes of this section, the term ‘business activity’ does not include any activity of a governmental entity or of any other organization which is exempt from tax under this chapter.

“(d) Deductions.—

“(1) In general.—The deductions specified in this subsection are—

“(A) the cost of business inputs for the business activity,

“(B) wages (as defined in section 3121(a) without regard to paragraph (1) thereof) which are paid in cash for services performed in the United States as an employee, and

“(C) retirement contributions to or under any plan or arrangement which makes retirement distributions (as defined in section 63(e)) for the benefit of such employees to the extent
such contributions are allowed as a deduction under section 404.

“(2) Business inputs.—

“(A) In general.—For purposes of paragraph (1), the term ‘cost of business inputs’ means—

“(i) the amount paid for property sold or used in connection with a business activity,

“(ii) the amount paid for services (other than for the services of employees, including fringe benefits paid by reason of such services) in connection with a business activity, and

“(iii) any excise tax, sales tax, customs duty, or other separately stated levy imposed by a Federal, State, or local government on the purchase of property or services which are for use in connection with a business activity.

Such term shall not include any tax imposed by chapter 2 or 21.

“(B) Exceptions.—Such term shall not include—
“(i) items described in subparagraphs (B) and (C) of paragraph (1), and
“(ii) items for personal use not in connection with any business activity.
“(C) EXCHANGES.—For purposes of this section, the amount treated as paid in connection with the exchange of property or services is the fair market value of the property or services exchanged, plus any money paid.
“(e) SPECIAL RULES FOR FINANCIAL INTERMEDIATION SERVICE ACTIVITIES.—In the case of the business activity of providing financial intermediation services, the taxable income from such activity shall be equal to the value of the intermediation services provided in such activity.
“(f) EXCEPTION FOR SERVICES PERFORMED AS EMPLOYEE.—For purposes of this section, the term ‘business activity’ does not include the performance of services by an employee for the employee’s employer.
“(g) CARRYOVER OF CREDIT-EQUIVALENT OF EXCESS DEDUCTIONS.—
“(1) IN GENERAL.—If the aggregate deductions for any taxable year exceed the gross active income for such taxable year, the credit-equivalent of such excess shall be allowed as a credit against the tax
imposed by this section for the following taxable year.

“(2) CREDIT-EQUIVALENT OF EXCESS DEDUCTIONS.—For purposes of paragraph (1), the credit-equivalent of the excess described in paragraph (1) for any taxable year is an amount equal to—

“(A) the sum of—

“(i) such excess, plus

“(ii) the product of such excess and the 3-month Treasury rate for the last month of such taxable year, multiplied by

“(B) the rate of the tax imposed by subsection (a) for such taxable year.

“(3) CARRYOVER OF UNUSED CREDIT.—If the credit allowable for any taxable year by reason of this subsection exceeds the tax imposed by this section for such year, then (in lieu of treating such excess as an overpayment) the sum of—

“(A) such excess, plus

“(B) the product of such excess and the 3-month Treasury rate for the last month of such taxable year,

shall be allowed as a credit against the tax imposed by this section for the following taxable year.
“(4) 3-MONTH TREASURY RATE.—For purposes of this subsection, the 3-month Treasury rate is the rate determined by the Secretary based on the average market yield (during any 1-month period selected by the Secretary and ending in the calendar month in which the determination is made) on outstanding marketable obligations of the United States with remaining periods to maturity of 3 months or less.

“SEC. 60C. TAX ON NONCASH COMPENSATION PROVIDED TO EMPLOYEES NOT ENGAGED IN BUSINESS ACTIVITY.

“(a) IMPOSITION OF TAX.—There is hereby imposed on every employer of an employee to whom this section applies and who makes an election to be taxed under this part a tax equal to—

“(1) 19 percent of the value of excludable compensation provided during the calendar year by the employer for the benefit of employees to whom this section applies in the case of the first 2 calendar years beginning with the calendar year for which the election under section 60 is made, and

“(2) 17 percent of such excludable compensation during the calendar year in the case of all cal-
endar years subsequent to the calendar years de-
scribed in paragraph (1).

“(b) LIABILITY FOR TAX.—The tax imposed by this
section shall be paid by the employer.

“(c) EXCLUDABLE COMPENSATION.—For purposes
of subsection (a), the term ‘excludable compensation’
means any remuneration for services performed as an em-
ployee other than—

“(1) wages (as defined in section 3121(a) with-
out regard to paragraph (1) thereof) which are paid
in cash,

“(2) remuneration for services performed out-
side the United States, and

“(3) retirement contributions to or under any
plan or arrangement which makes retirement dis-
tributions (as defined in section 63(c)).

“(d) EMPLOYEES TO WHOM SECTION APPLIES.—
This section shall apply to an employee who is employed
in any activity by—

“(1) any organization which is exempt from
taxation under this chapter, or

“(2) any agency or instrumentality of the
United States, any State or political subdivision of
a State, or the District of Columbia.”.
(b) CLERICAL AMENDMENT.—The table of parts for subchapter A of chapter 1 of such Code is amended by adding at the end the following new item:

"PART VIII. FREEDOM FLAT TAX".

(e) EFFECTIVE DATE.—The amendments made by this title shall apply to taxable years beginning after December 31, 2005.

SEC. 3. REPEAL OF ESTATE AND GIFT TAXES.

(a) IN GENERAL.—Subtitle B of the Internal Revenue Code of 1986 is hereby repealed.

(b) EFFECTIVE DATE.—The repeal made by subsection (a) shall apply to the estates of decedents dying, and gifts and generation-skipping transfers made, after December 31, 2005.

SEC. 4. SUPERMAJORITY REQUIRED TO CONSIDER REVENUE MEASURE.

A bill, joint resolution, amendment to a bill or joint resolution, or conference report that—

(1) includes an increase in the rates of tax specified in section 60A(a) or 60B(a) of the Internal Revenue Code of 1986 (as amended by this Act), or

(2) reduces the standard deduction, as defined in section 60A(c) of such Code (as so amended), or the deductions specified in section 60B(d) of such Code (as so amended),
may not be considered as passed or agreed to by the
House of Representatives or the Senate unless so deter-
mined by a vote of not less than two-thirds of the Members
of the House of Representatives or the Senate (as the case
may be) voting, a quorum being present.