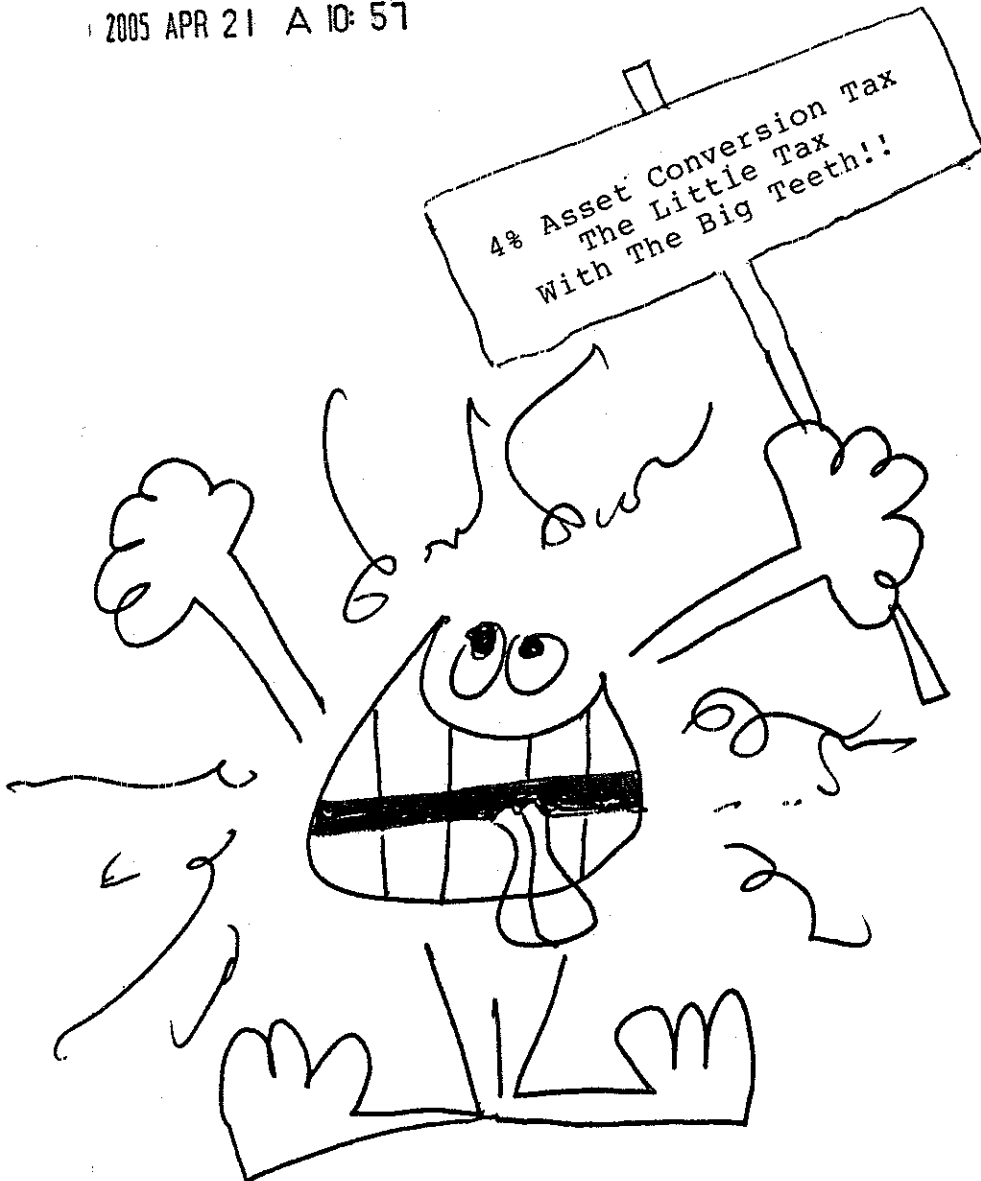


PRESIDENT'S ADVISORY
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ON FEDERAL TAX REFORM

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Robert H. Showen
Individual

1409 Ptarmigan Drive
Walnut Creek, CA 94595-4137

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(925) 939-4412

4% ASSET CONVERSION TAX

Let me start with some credentials since anyone who advocates the complete restructure of our entire federal, state and local tax systems has to be thought of initially as somewhat of a crackpot. I am a graduate of Stanford University in California and Southern Methodist University Law School in Texas, where I served as Editor-in-Chief of the Southwestern Law Journal. I began my tax practice in 1955 with the Department of Justice as a part of Attorney General Herbert Brownell's honor graduate recruitment program, and have been engaged in a tax practice for the last fifty years.

Second, let us dispel a couple of half-truths. At the Panel's meeting in San Francisco, I was disappointed to hear some very capable people make remarks like "corporations don't pay taxes, only people pay taxes". This is hogwash. Of course corporations do, and should continue to, pay billions of dollars in taxes (about 4% of their gross receipts), but these tax expenses, just like any other expense of doing business, are taken into consideration in determining the price of the goods or services that the corporation sells to other corporations or to people. The opposite also occurs. The newspapers recently contained articles about a CEO who entered into a 38 million dollar compensation agreement with a large oil corporation. You

can be sure that a very strong motivation in the mind of that CEO was the realization that he probably would have to pay about half of his compensation in federal, state and local income taxes, sales taxes, property taxes, telephone taxes, airline taxes, hotel taxes, etc., etc. The second half-truth is "taxing a corporation, and then taxing its shareholders on dividends is double taxation". More hogwash. Actually it is probably two dozen taxation because the corporation probably paid at least a dozen taxes, and, as was the case with the CEO above, the shareholder will pay another dozen taxes on the dividends. Many years ago, the University of Chicago did a study tracing 591 separate taxes into a single loaf of bread. Now let us proceed into a more rational and fair tax system.

A. DESCRIPTION OF PROPOSAL - 4% ASSET CONVERSION TAX

(1) The Tax Base (Hybrid): According to The Tax Foundation estimates, the average U.S. taxpayer is now paying about 30% of his or her gross income on federal, state and local taxes (normally about 35% in years without large unemployment). The 4% Asset Conversion Tax will replace all of the federal, state and local tax systems with a single 4% tax on the conversion into cash of all assets, whether representing work or wealth. Because it is computed on a tax base about 50 times greater than the tax base that we presently use, the 4% Asset Conversion Tax will completely balance all federal, state and

local governmental budgets within one day, will pay off all federal, state and local governmental debts within two or three years, and will provide more than enough funds to solve the problems of the inadequately funded governmental services.

The last time, in 1997, that the Statistical Abstract of the U.S. reported the figure that is the tax base for the 4% Asset Conversion Tax it was for the year 1995 a total of almost 400 Trillion Dollars (Table 797 - Debits to Demand Deposits, All Banks: 397.6 Trillion Dollars). That same 1997 Statistical Abstract reported a 1995 U.S. Gross Domestic Product of 7.2 Trillion Dollars and a 1995 Market Value of All Sales, All Exchanges of 3.7 Trillion Dollars. Each of these items have increased substantially now, ten years later.

At the same time that the 4% Asset Conversion Tax increases taxes for governments it provides meaningful tax reform by reducing the total federal, state and local tax burden on the average family in the United States from the present 30% (or the normal 35%) of gross income all the way down to 4% of gross income - about a 90% reduction in total family taxes.

(2) Exemptions, Deductions, Credits & Exclusions: The 4% Asset Conversion Tax has absolutely no exemptions, deductions, credits or exclusions. Even the receipts of the federal, state and local governments will be subject to all of the provisions of the 4% ACT. If you permit any single exemption, deduction,

credit or exclusion, soon there will be a hundred of them, then a thousand of them, and before long we will find ourselves in the hopeless tax mess that we now experience.

(3) Tax Rate(s): For honest taxpayers the tax rate is four percent (4%), no matter how little or how much is involved in the transaction. For negligent taxpayers the tax rate is forty percent (40%). For criminal taxpayers the tax rate is four hundred percent (400%). If the negligent taxpayer, or the criminal taxpayer, is an organization, then a like tax (not reimbursable) shall be imposed on the chief executive officer, and a like tax (not reimbursable) shall be imposed on the chief financial officer, of any such organization.

(4) Distribution of the Tax Burden: If the 1995 ratio of Gross Domestic Product to Debits to Demand Deposits (referred to on page 3 of this presentation) still holds true today, then about two percent (2%) of the tax burden of the 4% Asset Conversion Tax would be represented by the conversion of work into cash and about ninety-eight percent (98%) of the tax burden of the 4% Asset Conversion Tax would be represented by the conversion of wealth into cash. With regard to relief for low-income individuals, it is hard to conceive of any situation in which the tax burden on a low-income individual would not be substantially lower under the 4% ACT than it is under all of our present tax systems. The total federal, state and local tax

burden under the 4% ACT on a person earning \$12,000 per year will be \$480. Under our present tax law systems, even if the low-income individual is able to avoid the net income taxes, he or she will face various employment taxes, sales taxes, property taxes, auto registration fees, gasoline taxes, telephone taxes, etc., etc. These various present taxes can substantially exceed the \$480 total 4% ACT taxes in short order.

(5) Treatment of Charitable Giving: The 4% Asset Conversion Tax has no deductions whatsoever, neither for charitable giving nor for any other reason. However, the 4% ACT offers a better hope for prospective charitable beneficiaries. Take churches, for example. Everyone presently recognizes that, subject to certain rules, a gift to a recognized church is deductible for net income tax purposes. However in 50 years of tax law practice I have never heard of a taxpayer who said "I want to give away \$80,000, and divide it equally among the forty different churches in our city." Deductibility is not the principal motivation in charitable giving to churches, the principal motivation is the belief in the message or the mission of the church. The better hope for churches and other prospective charitable beneficiaries offered by the 4% ACT is that in normal years the average taxpayer will have about 30% extra after-tax dollars from his or her income. As explained in the Proposed U.S. Constitutional Amendment attached, 10% out of

the extra 30% after-tax dollars will be invested directly in the taxpayer's personal retirement account(s) that can be invested in prudent investments chosen by the taxpayer, including but not limited to, stocks and bonds. That leaves 20% out of the extra 30% savings from the Asset Conversion Tax for charitable gifts, home loan payments, etc.

(6) Treatment of Home Ownership: As explained in the preceding paragraph about charitable giving, the 4% Asset Conversion Tax has no deductions whatsoever, neither for home loan interest nor for any other reason. However, the 4% ACT also offers a better hope for prospective home-owners. The 2004-2005 Statistical Abstract of the U.S. shows the annual median family income in the U.S. to be almost \$42,000. Assume that such median income family was paying \$1,000 per month to rent a home, and chooses to use that rent amount plus the entire 20% out of the extra 30% savings from the Asset Conversion Tax to make home loan payments of \$1,700 per month ($\$1,000 + \$42,000 \times 20\%/12$). At today's rates the \$1,700 monthly payment would support a typical 80% 30-year loan of \$280,000. Together with a typical 20% down payment of \$70,000, this would allow the median income family to purchase a \$350,000 home. While this would not allow the median income family to purchase a median priced home in the San Francisco Bay Area, it would more than allow them to purchase a new median-priced family home in most areas of the

U.S., which, according to the 2004-2005 Statistical Abstract of the U.S., costs only \$195,000.

7. Collection Method: Under the 4% ACT you will never again have to file a federal, state or local income tax return. Suppose you receive a check for \$100.00. When you deposit the check in your bank, your bank will put \$96.00 into your checking account and will send the remaining \$4.00 to the 4% ACT Central Collection Agency. The Collection Agency will then allocate your \$4.00 Asset Conversion Tax payment, together with the more than Fifteen Trillion Dollars of other 4% ACT payments that the Collection Agency will receive each year, among the federal, state and local governments in accordance with the formula contained in the attached Proposed U.S. Constitutional Amendment establishing the 4% Asset Conversion Tax, a five page document, rather than the current 17,000 page Internal Revenue Code. Annually all the federal, state and local tax systems now collect less than Five Trillion Dollars.

(8) Treatment of Businesses: All businesses will be treated exactly equally under the 4% Asset Conversion Tax. If you operate a jewelry store, you can be sure that your friendly competitor down the street, and all jewelry stores throughout the U.S., will also be paying 4% of their gross cash receipts under the 4% ACT.

B. IMPACT OF 4% ACT RELATIVE TO CURRENT SYSTEM

(1) Simplicity: Nothing can be more simple than a single-rate tax that eliminates the need for tax returns. Collecting the 4% ACT through the banking system provides for maximum transparency. It would require a criminal conspiracy between the bank and its depositor-taxpayer to avoid the 4% ACT, and there are very few bankers that would risk going to prison just to save a depositor-taxpayer 4% of the amount of a deposit. The ultimate stability is provided by establishing the 4% Asset Conversion Tax in an Amendment to the U.S. Constitution.

(2) Fairness: My pet complaint about our present net income tax system is the approximately 2,000% advantage given to corporations over individuals:

| Year | AGI | <u>Indivs</u> Tax | Tax/ AGI | AGI | <u>Corps</u> Tax | Tax/ AGI | Corps Advntg | Pres' Name |
|------|------------|----------------------|-------------|---------|---------------------|-------------|-----------------|---------------|
| End | \$\$\$\$\$ | \$\$\$\$\$ | AGI | Bil\$\$ | Bil\$\$ | AGI | | |
| 1956 | 4,568 | 556 | 12.2% | 680 | 21 | 3.1% | 394% | Eisen |
| 1960 | 5,224 | 651 | 12.5% | 724 | 22 | 3.0% | 417% | Eisen |
| 1964 | 6,132 | 726 | 11.8% | 968 | 27 | 2.8% | 421% | JK/LJ |
| 1968 | 7,585 | 1,045 | 13.8% | 1,350 | 37 | 2.7% | 511% | LBJ |
| 1972 | 11,789 | 1,537 | 13.0% | 1,895 | 40 | 2.1% | 619% | Nixon |
| 1976 | 15,600 | 2,201 | 14.1% | 3,637 | 50 | 1.4% | 1007% | N/Ford |
| 1980 | 22,935 | 3,389 | 14.8% | 6,361 | 62 | 1.0% | 1480% | Carter |
| 1984 | 21,520 | 3,698 | 17.2% | 7,136 | 52 | 0.7% | 2457% | Reagn |
| 1988 | 36,633 | 4,705 | 12.8% | 10,265 | 92 | 0.9% | 1422% | Reagn |
| 1992 | 31,945 | 5,491 | 17.2% | 11,742 | 102 | 0.9% | 1911% | Bush 1 |
| 1996 | 37,690 | 7,239 | 19.2% | 15,526 | 171 | 1.1% | 1745% | Clintn |
| 2000 | 49,202 | 10,127 | 20.6% | 20,606 | 204 | 1.0% | 2060% | Clintn |
| 2001 | 47,373 | 9,370 | 19.8% | 20,273 | 167 | 0.8% | 2475% | Bush 2 |

On the other hand, the 4% Asset Conversion Tax provides complete fairness in that all honest taxpayers are taxed at the same 4% rate. However, taxation under the 4% ACT is progressive because

about two percent (2%) of the tax burden of the 4% Asset Conversion Tax will be represented by the conversion of work into cash and about ninety-eight percent (98%) of the tax burden of the 4% Asset Conversion Tax will be represented by the conversion of wealth into cash, and wealth is concentrated in the very upper percentages of the U.S. population.

(3) Economic Growth and Competitiveness: With our stability and only a 4% ACT tax rate, it is conceivable that the U.S. might become the tax haven country for the world. Under the 4% ACT the average taxpayer will have about 30% extra after-tax dollars from his or her income. As explained in the Proposed U.S. Constitutional Amendment attached, 10% out of the extra 30% after-tax dollars will be invested directly in the taxpayer's personal retirement account(s). That leaves 20% out of the extra 30% savings from the Asset Conversion Tax for discretionary spending. Both the 10% investment portion and the 20% discretionary spending portion will be most beneficial to U.S. economic growth. So far as world competition is concerned, having the lowest total tax rate in the world, just 4%, certainly will be advantageous to the United States. However, the most important world competition factors will remain as the continued increase in the productivity of U.S. workers and the hopeful reduction of compensation levels of U.S. CEOs and other

executives to levels more comparable to their counterparts in other industrialized countries in the world.

(4) Compliance and Administration Costs: The compliance cost to taxpayers is almost nil. The administration costs to the federal, state and local governments should not exceed 10% of the current costs of the Federal Internal Revenue Service.

C. TRANSITION, TRADEOFFS & SPECIAL ISSUES

(1) Tradeoffs or Unequal Treatments: Since the heart of the 4% ACT is absolute equality, none of these items will occur.

(2) Impact of Transition: Since the 4% ACT is revenue positive rather than revenue neutral, the 4% ACT will cause the U.S. to transition from the world's greatest governmental debt nation to what will probably be the only nation in the world that is completely free of governmental debt.

(3) Abolition of Sovereign Immunity: Having a simpler and fairer tax system alone is not enough. Politicians make noble speeches about being "trustees of the taxpayers' funds", and half an hour later start to scream and fight like a flock of hungry buzzards fighting over a road kill. The last Section of the attached Proposed U.S. Constitutional Amendment abolishes the doctrine of sovereign immunity, and imposes actual trustee liability on all federal, state and local governments and their respective elected officials and other government employees.

AMENDMENT XXVIII - THE GOOD GOVERNMENT'S AMENDMENT

Section 1: Amendment XVI to the United States Constitution, and all provisions of the United States Constitution and its prior Amendments that are inconsistent with this Constitutional Amendment, are hereby repealed or revised to be consistent with this Constitutional Amendment. Other than federal import duties, there shall be only one federal, state or local tax in the United States or its states, districts or territories, imposed upon the world-wide cash receipts of its individual citizens or resident aliens, or imposed upon the United States, or its states, districts or territories, source cash receipts of any organization (such as a corporation, partnership, or any other form of association, organized inside or outside of the United States and whether organized for profit or not for profit) doing business in the United States, as doing business is hereafter defined by federal statutes, i.e.:

(a) A four percent (4%) Asset Conversion Tax on the gross value of the recipient's conversion into cash of all assets, whether representing work or representing wealth; and

(b) A forty percent (40%) Asset Conversion Tax on the gross value of each side of any barter transaction, or on the recipient's side of any other non-barter transaction, that has not been reported and on which the four percent (4%) Asset Conversion Tax has not been paid. If either or both sides of any such barter transaction, or on the recipient's side of any other non-barter transaction, is an organization, then a like tax (not reimbursable) shall be imposed on the chief executive officer, and a like tax (not reimbursable) shall be imposed on the chief financial officer, of any such organization; and

(c) A four hundred percent (400%) Asset Conversion Tax on the gross value of each side of any barter transaction, or on the recipient's side of any other non-barter transaction, that has not been reported and on which the four percent (4%) Asset Conversion Tax has not been paid on the gross value of each side of any barter transaction, or on the recipient's side of any other non-barter transaction, that has not been reported and on which the four percent (4%) Asset Conversion Tax has not been paid, or any other transaction, entered into willfully attempting in any manner to evade or defeat any tax imposed by this Amendment XXVIII or the payment thereof. If either or both sides of any such barter transaction, or on the recipient's side of any other non-barter transaction, is an organization, then a like tax (not reimbursable) shall be imposed on the chief executive officer, and a like tax (not reimbursable) shall be imposed on the chief financial officer, of any such organization.

Section 2: There shall be no exemptions, deductions, preferential rates, credits, rebates or any other forms of reductions with respect to any Asset Conversion Tax.

Section 3: No tax returns shall be required of any individual or organization subject to the Asset Conversion Tax. The Asset Conversion Tax shall be collected and remitted daily, at the end of each business day, to the Central Collecting and Disbursing Agency as cash is deposited into the taxpayer's checking account at an Authorized Bank. All cash must be first deposited into an Authorized Bank, and each bank doing business in the United States, or its states, districts or territories, shall require that all checks or other transfers of funds drawn on such bank must be first deposited into an Authorized Bank.

Section 4: The tax revenues from the Asset Conversion Tax shall be distributed in the following order:

(a) The federal government will receive daily, within seven calendar days after their receipts by the Central Collecting and Disbursing Agency, $1/365^{\text{th}}$ ($1/366^{\text{th}}$ in leap years) of 120% of its budget in effect on February 8, 2005, the date of the introduction of this Constitutional Amendment, plus the amount necessary to pay off its entire federal governmental indebtedness evidenced by a bond, note, bill or similar document in eighteen approximately equal installments over the eighteen months following the end of the calendar month in which this Constitutional Amendment becomes ratified. The portion of the tax revenues relating to the 120% of the current budget shall be automatically adjusted for the calendar year 2005 and each successive calendar year forever thereafter by the Consumer Price Index adjustments described in Section 7 and to reflect the increases or decreases in the population of the United States of America as determined in the most recent previous national census completed by the U.S. Census Bureau. The balance of the revenues from the Asset Conversion Tax will be distributed daily, within seven calendar days after their receipts by the Central Collecting and Disbursing Agency, to the various states, federal districts and territories on the basis of their respective populations as determined in the most recent previous national census completed by the U.S. Census Bureau, in the following proportions:

(b) Each state, federal district or territorial government will receive daily, within seven calendar days after their receipts by the Central Collecting and Disbursing Agency, $1/365^{\text{th}}$ ($1/366^{\text{th}}$ in leap years) of 120% of its budget in effect on February 8, 2005, the date of the introduction of this Constitutional Amendment, plus the amount necessary to pay off

its entire governmental indebtedness evidenced by a bond, note, bill or similar document in eighteen approximately equal installments over the eighteen months following the end of the calendar month in which this Constitutional Amendment becomes ratified. The portion of the tax revenues relating to the 120% of the current budget shall be automatically adjusted for the calendar year 2005 and each successive calendar year forever thereafter by the Consumer Price Index adjustments described in Section 7 and to reflect the increases or decreases in their respective populations as determined in the most recent previous national census completed by the U.S. Census Bureau.

(c) The remaining balance of the tax revenues from the Asset Conversion Tax shall be distributed daily, within seven calendar days after their receipts by the respective states, federal districts or territories, among the various counties within a given state, federal district or territory on the basis of such counties respective populations as determined in the most recent previous national census completed by the U.S. Census Bureau. Revenues in excess of those determined by such counties to be appropriate to provide for county-wide services and projects shall be distributed daily, within seven calendar days after their receipts by such counties, among the various cities, districts and unincorporated areas within such counties on the basis of the respective populations served by such cities, districts and unincorporated areas as determined in the most recent previous national census completed by the U.S. Census Bureau.

Section 5: No federal, federal district or territory, state or local, government or governmental agency shall impose or continue to enforce any additional new taxes (other than federal import duties) or incur any indebtedness evidenced by a bond, note, bill or similar document after the date this Constitutional Amendment becomes ratified. Any such action shall be deemed to be an act of treason, within the meaning of Article III Section 3 of the United States Constitution, by the governmental employees or other individuals involved.

Section 6: All private and governmental employers in the United States and its states, districts or territories shall, within seven calendar days after the end of each pay period, remit to each employee's personal retirement account(s) designated by such employee, a percentage designated by such employee (not less than ten percent) of the gross compensation otherwise payable to such employee for such pay period. Employees may change, at least once each calendar quarter, their designations to their employers of either or both of the

specified percentages to be remitted by the employer or the names of the employee's personal retirement account(s) to which remittances are to be made by the employer.

Section 7: The federal Social Security retirement system shall be phased out over a twenty-five year period commencing January 1, 2010. However, Qualified Employees who have retired before the dates specified below, and their beneficiaries, shall continue to receive for their entire lifetimes, the percentage of their Social Security retirement benefits specified below:

| <u>Qualified Employees Retired</u> <u>Before January 1st of</u> | <u>Percentage</u> <u>Of Benefits</u> |
|---|---|
| 2010 | 100% |
| 2011 | 96% |
| 2012 | 92% |

The four percent reduction each calendar year shall continue each successive calendar year until the percentage of Social Security retirement benefits is zero percent. After February 8, 2005, the date of the introduction of this Constitutional Amendment, no changes shall be made in the attained ages required for normal retirement or early retirement, and any reductions in Social Security payments based upon earned income or outside income are eliminated effective as of the date this Constitutional Amendment becomes ratified. The amount of benefits payable for the calendar year 2005 shall be automatically adjusted up or down in proportion to the ratio of the Consumer Price Index for All Urban Consumers, U.S. City Average, All Items for September 2004 over such Index for September 2003. A similar automatic annual adjustment shall be made for each successive calendar year thereafter until the date when the last surviving Social Security retirement benefit recipient dies.

Section 8: To encourage the accomplishment of governmental functions through private independent contractors selected under competitive bidding, the number of government employees in each level of government (federal, state and local) shall be reduced each calendar year after the calendar year 2005 on the basis of 10% declining balance depreciation rounded off to the nearest whole individual.

Section 9: To encourage the consolidation of local governmental functions at the county level, government employees of cities or districts within the county that are consolidated as employees of the county itself, shall not be included in the total of county government employees in any given county for the

calendar year in which such consolidation occurs. Any government (federal, state or local) that fails to meet the foregoing reductions in government employees for any calendar year shall not receive any share of the Asset Conversion Tax for the succeeding five calendar years. Any such failing government's share of the Asset Conversion Tax will go to, and such failing government's services will be performed by, the next superior governmental authority for such succeeding five calendar years. For example, a failing city government would be replaced by the county government in which the city is located, a failing county government would be replaced by the state government in which the county is located and a failing state government would be replaced by the federal government. If the failing government is the federal government, then within not more than ninety days after the end of the calendar year for which the federal government fails to meet the foregoing reductions in government employees, special elections shall be held to replace all of the elected federal officials with new and different individuals, but the elected federal officials who failed to meet the foregoing reductions in government employees will continue to serve until their new and different individual successors are so elected.

Section 10: The doctrine of sovereign immunity of federal, state and local governments within the United States and its districts and territories, and their respective elected officials and other government employees, is hereby abolished. The responsibilities and liabilities of such governments, and their respective elected officials and other government employees, shall be determined under the most restrictive laws applicable to trustees or other fiduciaries in the state, district or territory in which the alleged improper action has occurred.