

The Tax Council

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April 29, 2005

The Honorable Connie Mack
Chairman
The President's Advisory Panel on Federal Tax Reform
1440 New York Avenue N.W., Suite 2100
Washington, DC 20220

Dear Mr. Chairman:

On behalf of the members of The Tax Council, I thank the President for creating the Advisory Panel on Federal Tax Reform and congratulate you on your appointment as Chairman. Your mission is extremely important and we applaud the Advisory Panel for the thorough and comprehensive manner in which it is fulfilling its responsibility.

Because the issues with which you are dealing are critical to all of our members, The Tax Council has adopted the enclosed principles on tax reform. As the Advisory Panel carefully examines the many complex and controversial aspects of federal tax reform, we urge you to consider them in conjunction with these principles.

We look forward to working with the Advisory Panel as the process moves forward and invite you or any members to contact us if additional information is needed.

Sincerely,



Kenneth Petrini
Chairman, Tax Policy Committee
The Tax Council

Enclosure

PRESIDENT'S ADVISORY
PANEL
ON FEDERAL TAX REFORM
2005 APR 30 P 3:32

THE TAX COUNCIL FUNDAMENTAL TAX REFORM

Tax Policy

Tax policy, especially as it applies to business, has a vital impact on economic expansion. Appropriate tax policy rewards individuals and businesses to continue to foster growth and technological advancement while retaining meaningful incentives for those at the downside of the business cycle so as not to exacerbate cyclical weakness. It must also reflect the global marketplace and allow business to compete abroad while not impeding foreign investment into the United States

Specific Principles for Change

Meet most tests of equity. In general, the tax system should be broadly based, should treat similar types of taxpayers the same (Horizontal Equity), and those with greater ability to pay should have tax burdens at least equal to those with less ability to pay (Vertical Equity).

Provide sufficient revenues. Taxes should be levied at levels sufficient to support the efficient and effective operation of government services deemed necessary by business and citizens. Such a system reflects that:

- Tax receipts are consistent over time.
- An appropriate balance exists among major tax sources.
- Taxes are predictable by business and citizens.

Be efficient in its administration. The administration of the tax system should minimize needless cost and be fair in application. A system which is expensive to comply with or which treats certain taxpayers unfairly in practice is inefficient.

Be simple in structure, unambiguous in application, and understandable to taxpayers. Simplification and increased understandability of the tax system lowers administrative costs and increases voluntary compliance. Compliance costs add to the cost of doing business without adding to the government's revenue collection.

Tax Reform

Any fundamental tax reform should:

1. Allow U.S. companies to compete in the global marketplace.

The current U.S. tax system was developed at a time when domestic and foreign business labels had meaning. Today, many business models require a global presence. The global marketplace must be reflected in any business tax system. Today's U.S. tax laws not only make it difficult for U.S. companies to compete beyond U.S. borders but also can render U.S. companies uncompetitive at home.

2. The business sector cannot be used as the source of funding cuts to individuals.

It is not sufficient that tax reform be revenue neutral. It should also avoid significant transfers of taxation onto the business community. While increased business tax burdens can be politically expedient, they can produce severe economic dislocations and ultimately harm individuals through higher prices, stagnant economic growth and job losses at home, and can hamper investment in business through reduced return to shareholders.

3. Any fundamental change requires appropriate transition rules.

Businesses have many carryover tax attributes (NOL's, foreign tax credits, charitable contribution carryforwards, deferred tax liability or assets) that represent timing issues. In a perpetual tax system, these attributes are expected to be used or imposed, as the case may be. Fundamental change that does not take such matters into account can effectively eliminate valuable property rights represented by these tax attributes, leading to unfair treatment of and among businesses.

4. Reduce the statutory tax rate facing corporations.

The U.S. corporate tax rate is the third highest (including state and local taxes) among all developed nations (OECD 2003). A reduction in the statutory rate can help make U.S. business more attractive as an investment. However, any rate reduction must be protected against subsequent tinkering that leaves rates back at historical levels while applying to a broader base.

5 Improve Access to the Capital Markets.

The taxation of dividends and capital gains, along with the tax treatment of interest, can greatly affect the flow of capital and, hence, the cost of business to access such capital. A system that avoids double taxation of employed capital and supports economic growth can increase the competitiveness of U.S. business and lead to increased tax revenues through sustained growth. A tax system that heavily taxes business capital reduces the return to investors, which discourages growth and leads to lower tax revenue in the long run.

6. Minimize Compliance Costs.

Increased costs grow out of tax complexity. These can be in the form of increased compliance costs. There is probably no tax return remotely as complex or costly as a multinational corporation's Form 1120. Costs are also found in compelling or restricting ways that multinationals must be structured to avoid incurring additional taxes under a complex tax code. These issues of complexity create real economic costs that are either passed on to consumers or labor, or reduce the return to investors.

7 Encourage Capital Spending.

Pro-growth tax reform should include a continuation of the movement towards expensing of capital purchases. The current Code's overly long depreciation lives discourage investment in American productivity and competitiveness. Enhanced expensing and/or accelerated depreciation should be available to all companies, regardless of size, and should not effectively be rendered unavailable to AMT taxpayers or producers of long lead-time items.