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## CHAIRMAN RANGEL'S TAX OVERHAUL

# THE DEMOCRATS' TRUE INTENTIONS

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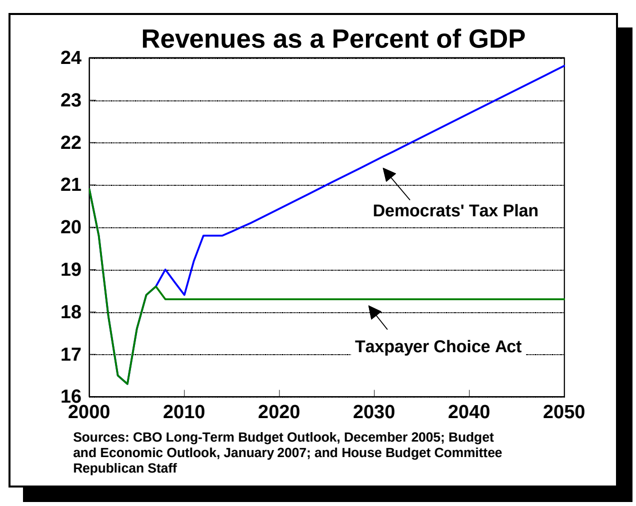
The tax overhaul plan released today by Ways and Means Committee Chairman Rangel finally reveals the true Democratic strategy: a $3.5-trillion tax increase over 10 years, and ever-increasing tax burdens thereafter. Chairman Rangel's candor contrasts with the constant denials of other Democratic leaders, but the bottom line is the same: the Majority's tax plan is almost guaranteed to smother economic growth and competitiveness at a time when the United States most needs them. Key features of the plan are the following:

- **Trades One Bad Tax Hike for Many Others.** The plan is based on a grossly flawed premise: it assumes that all the revenue from *unintended* tax increases is legitimate, no matter how unrealistic. Hence, while the plan repeals the alternative minimum tax [AMT], it *still raises other taxes to collect the $841 billion* that expansion of the AMT would impose. The plan also assumes (but does not mention) the expiration of tax relief provisions enacted in 2001 and 2003, resulting in marginal tax rate increases for all income-tax payers. In all, the plan raises taxes by $3.5 trillion over 10 years, *the largest individual income tax increase in history*.

  This is the clearest example to date of how the Democrats' pay-as-you-go [PAYGO] rule is a formula for higher taxes. It demands they "pay for" simply keeping tax burdens the same as they are today – *by raising taxes*. This directly contradicts the Majority's claims, during this year's budget debate, that they intended to protect "middle-income" tax relief.

- **Vastly Expands the Reach of Government.** Over the long term, the Majority's artificially inflated revenue path rises to nearly 24 percent of gross domestic product [GDP] by mid-century – compared with the historical range of about 18.3 percent of GDP (see chart). In other words, the Federal Government would consume about one-fourth all U.S. economic resources – and doubtless the Democrats would spend it all. This is the true intent of the Democrats' fiscal plan.




  In contrast, the Taxpayer Choice Act – recently proposed by Representatives Ryan, Hensarling, Campbell, and Bachmann –

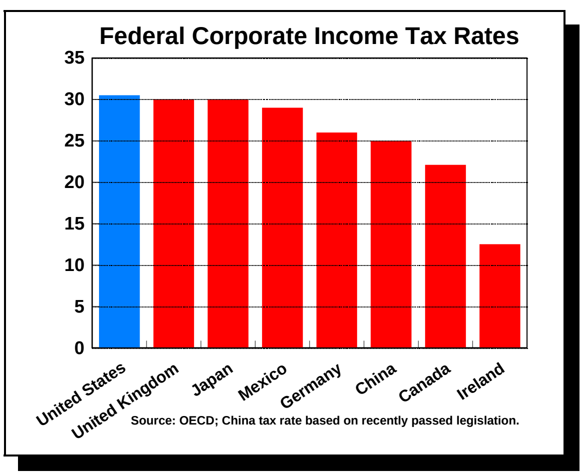
simplifies individual income taxes and eliminates the AMT, while still holding total tax revenue below 19 percent of GDP.

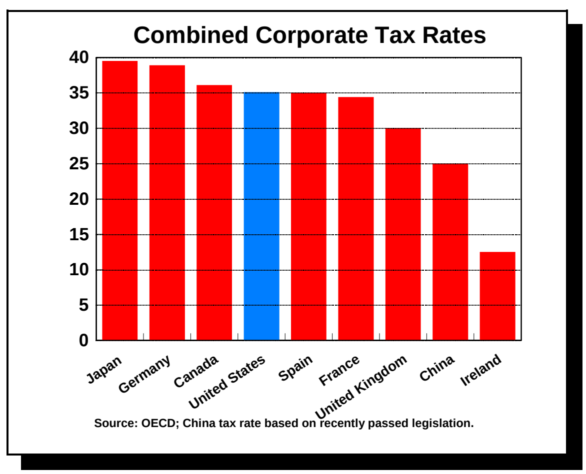
- **Raises Taxes on Small Businesses.** To offset the $841 billion of illegitimately assumed AMT revenue (including 2007), the plan would impose a 4-percent surtax that it describes euphemistically as a "limitation of benefits of individual AMT repeal." Specifically, the provision imposes the surcharge on adjusted gross income [AGI] above $150,000 for single filers and $200,000 for joint filers. The surcharge increases to 4.6 percent for incomes over $500,000. This proposal increases taxes by approximately $832 billion over 10 years.

  The surtax constitutes an assault on small businesses (i.e. non-corporations), most of which pay individual income tax rates on their business income. When coupled with the expiration of the 2001 and 2003 tax relief provisions, the surcharge would effectively push the highest income tax rate from its current level of 35 percent to 44.2 percent – an increase of 26 percent. Roughly 75 percent of the taxpayers affected by this top tax rate are job-producing small businesses – S-corporations, partnerships, and sole proprietorships – according to the U.S. Treasury. Recent economic research shows that an increase in top income tax rates will dissuade these businesses from investing, hiring more workers, and paying higher wages. That is significant because small businesses employ roughly half of the private labor force and create approximately seven out of every 10 new jobs. By some measures, small businesses account for more than half of GDP.

- **Widens the Gap Between Large and Small Businesses.** Taken as a whole, this tax plan would increase, to nearly 14 percentage points, the disparity between the Federal corporate income tax rate and the top rate paid by small businesses (which is the top individual income tax rate). Small businesses would pay a total top rate of 44.2 percent, while large corporations, such as IBM and Exxon, would pay a rate of 30.5 percent.

- **Fails to Enhance U.S. Competitiveness.** The proposal would lower the Federal corporate tax rate from 35 percent to 30.5 percent, but the overall benefit would be minimal. A U.S. Federal corporate rate of 30.5 percent would still be higher than those of



Germany (26 percent), Canada (22 percent), and the United Kingdom (30 percent). It is also higher than that of the rapidly growing market in China (25 percent), and the proven success story of Ireland (12.5 percent).

Most international comparisons, however, focus on a country's *combined* corporate tax rate (Federal plus State and local). At 39 percent, the U.S. currently has the second highest tax rate in the Organization for Economic Cooperation and Development [OECD]. The plan would simply lower the U.S. combined corporate rate to 35 percent, still the fourth highest in the OECD – and above European countries such as Spain, France, and Italy.

It is widely agreed that elevated corporate tax rates hinder U.S. competitiveness by making the country a less desirable destination for investment and jobs. By deterring potential investment, the tax restrains economic growth and job creation. The U.S. tax rate differential with other countries also fosters a variety of complicated multinational corporate behaviors intended to avoid the tax – profit-shifting, corporate inversions, and transfer pricing – which have the effect of moving the tax base offshore, costing jobs and decreasing corporate revenue.