U.S. SENATE COMMITTEE ON

Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

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Opening Statement of Senator Chuck Grassley
Senate Finance Committee Hearing:
"Our Business Tax System: Objectives, Deficiencies, and Options for Reform"
Wednesday, Sept. 20, 2006

The U.S. economy is fueled by U.S. businesses, from the smallest family business to the largest multinational corporation. President Bush has called our economy the envy of the world, and I think he's right. Our GDP growth, productivity, low inflation and unemployment are unmatched among developed economies. But I haven't heard anyone claim to be envious of our business tax system. The primary objective of our business tax system is to promote sensible tax policy. By that I mean it should equitably raise an appropriate level of revenues, minimize tax-induced distortions to legitimate business decision making, and be as simple as possible.

Some hard-core economists may disagree, but another objective of our business tax system should be to promote sensible non-tax policies. The system should provide effective, transparent, and easy-to-administer incentives for appropriate business activities. But we should keep in mind that targeted incentives increase the tax burden on everybody else. The President's Tax Reform Panel got it right, when it said, quote, that "a rational system would favor a broad tax base, providing special treatment only where it can be persuasively demonstrated that the effect of a deduction, exclusion, or credit justifies higher taxes paid by all taxpayers," end quote. I suspect many of the business tax expenditures in the code today would fail that test if the realities of politics were set aside.

Another non-tax policy that we hear much talk of is competitiveness. We have heard about how we need to change our business tax system because of competitiveness. But it is not always clear what is meant by the term competitiveness. For example, a large multi-national may think of it as being competitive with foreign businesses in foreign markets. A family business may think of it being competitive with a large multi-national corporation in a local domestic market. American workers may think of it in terms of being able to compete for a job. A policy maker may think of it in terms of making the U.S. more competitive with other countries in attracting investment that leads to new jobs and better jobs.

A cynic might say that competitiveness is just a more palatable code word for cutting taxes. In a sense, that's right. Taxes, by definition, represent a transaction cost of doing business. From a business person's perspective, it's a sunk cost, with no expected rate of return. But it's a fact of life that we must fund our government, and taxing business activity, in some form, is necessary. Our goal, therefore, is to minimize as much as possible the tax system's interference with rational business behavior.

Our current business tax system is indisputably complex. But it is equally indisputable that businesses operate in a complex world. There is wide variation in businesses, in terms of size and complexity, and addressing this variation is one challenge our business tax system faces. Many businesses engage in complex transactions, relationships, and legal structures in a global marketplace. Globalization creates challenges to our business tax system. U.S. businesses operate in global markets for capital, customers, suppliers, competitors, and business partners. A related challenge is the global integration of multinational corporations and the increasing prominence of intangible assets in driving economic profit.

Our tax system needs to fairly and efficiently address the realities of business complexity and globalization. In August, we had a hearing to kick-off this committee's look at tax reform. We heard testimony from members of the President's Advisory Panel on Federal Tax Reform who took the first step at tackling the problems of our overall tax system. Today, we'll focus on our business tax system, which covers large publicly traded corporations and family businesses that are taxed at the individual level. It is important that we examine business tax reform as a whole before focusing on a single aspect of reform. We need to get the big picture first. I expect this hearing to serve as a platform on which to base future hearings that will examine specific aspects of business tax reform in greater depth as we work toward reforming the tax code. In this hearing, we will examine the objectives of our business tax system, challenges to our business tax system, deficiencies of our business tax system, and reform options to address some of those deficiencies.

The Honorable David Walker, Comptroller General of the Government Accountability Office will put business taxes in the context of our overall budget situation and offer guidelines for policymakers to follow in pursuing business tax reform. Dr. Robert Carroll, Deputy Assistant Secretary for Tax Analysis at Treasury, will discuss the Treasury's views on the need for business tax reform, characteristics of an optimal business tax system, and trade-offs that need to be considered in the context of business tax reform. Treasury has not yet made its tax reform recommendations to the President, and I don't expect Dr. Carroll to discuss any Treasury-endorsed tax reform plan. The Honorable Charles Rossotti, Senior Advisor at the Carlyle Group, and former IRS Commissioner and a member of the President's Advisory Panel on Federal Tax Reform, will discuss inefficiencies of our current business tax system and the principles he thinks are essential to making the system simpler, fairer, and more efficient. Dr. Thomas Neubig, National Director, Quantitative Economics and Statistics at Ernst and Young, will discuss reasons why corporations should prefer a lower tax rate to targeted tax reductions. Mr. David Bernard, International President of Tax Executives Institute and Vice President of Tax and Real Estate for Kimberly-Clark Corporation, will give views on tax reform from the perspective of large, multinational business enterprises. Mr. Jeff Johannesen, Managing Director at RSM McGladrey in Des Moines, Iowa, will give views on tax reform from the perspective of small and mid-size businesses. I'd like to offer a warm welcome to Mr. Johannesen, who is also a constituent. His firm was started in 1926 as a seven-person office in Cedar Rapids Iowa. Today, RSM McGladrey employs more than 7,000 people in over 130 offices in 25 states.

Closing Statement of Senator Chuck Grassley
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In closing, I'd like to thank each of the witnesses for taking the time to educate members of this committee on a broad range of business tax issues. As I said at the beginning of this hearing, it is important that we examine business tax reform as a whole before focusing on a single aspect of reform. We need to get the big picture first, and I think we did.

Tax reform will take a bipartisan, national consensus. I think the consensus is there that the business tax system is in desperate need of reform. But we need to start building consensus on how to do it. The theme of lowering rates and broadening the base is easy to agree with in theory. The tough part will be figuring out how low and how broad. This committee will continue down the path of tax reform. This hearing sets the stage for future hearings that will examine specific aspects of business tax reform in greater depth as we work toward reforming the tax code.