

# NEW DEMOCRAT COALITION PRINCIPLES FOR COMPREHENSIVE TAX REFORM

Innovation, Competitiveness and Tax Reform Task Force

In the past 25 years, the global economy has become increasingly dynamic and interconnected. To help American businesses and workers succeed, our nation's system of taxation needs to evolve to reflect the challenges facing modern businesses and opportunities for growth as well as address how individuals earn and utilize their income

Since 1986, Congress and various Administrations have added layer upon layer of targeted – and often temporary – tax benefits to the code. While a number have merit, many have proven ineffective in spurring economic growth and innovation, and the end result is a system that is mired with inefficiencies and instability, imposes burdensome compliance costs that impede economic growth and impairs the ability of businesses and individuals to plan ahead and compete. With debt levels at historic highs and threatening future economic stability, it is further imperative that tax reform create a pro-growth environment. An improved tax code will provide certainty for individuals and businesses as well as a stable and efficient source of revenue for essential government investments and services.

In this document, the New Democrat Coalition has outlined basic principles for reforming our nation's system of taxation using the following criteria:

- **Growth** – The economic rationale and need for the tax
- **Simplicity** – The costs of complying with and collecting the tax
- **Equity** – The fairness of the tax with respect to who bears the burden
- **Efficiency** – The impact of the tax on economic activity

By simplifying our tax code to create a more efficient, equitable and rational system we can allow individuals and businesses to prosper while restoring fiscal order.

## NDC BASIC PRINCIPLES

**Principle 1: Reform both individual and corporate income taxation.** Tax reform has the potential to improve American competitiveness and create jobs. The individual and corporate code should be reformed in tandem to ensure the most seamless, equitable code possible. With less than 10% of businesses filing as corporations for purposes of the Internal Revenue Code, limiting reform to corporate taxation may leave some small businesses behind and retain overlapping and inconsistent rules for corporations, non-corporate businesses, and individuals in place and unreconciled. As we reform the tax code to incentivize growth, we must avoid unduly shifting the tax burden on to those taxpayers with lesser means. Such taxpayers are subject to a number of other taxes (sales, payroll, property, and fuel taxes), which are regressive in nature. We affirm the principles of a progressive income tax code, which helped create and sustain a strong American middle class. We must maintain progressivity of the code to reflect individuals' ability to pay.

**Principle 2: Promote international competitiveness.** In an increasingly dynamic global economy, American workers and businesses must have a tax structure that allows them to compete, succeed and prosper. Our tax system should unleash the competitive potential of Americans at home and abroad by encouraging new investments in American technologies and products, promoting exports of American

products and services, and removing unnecessary tax burdens that disadvantage American companies on the global stage. To compete internationally, we need to lower the marginal corporate tax rates and create a system that spurs the creation and retention of new intellectual property (IP) intensive and highly technical jobs while also bringing back to U.S. soil manufacturing jobs that have been sent overseas. To do this, we should ease access to capital by encouraging U.S. companies to bring home more of their earnings to invest those dollars in domestic job creation. By lowering corporate rates to a competitive level internationally, we can also reduce or remove tax benefits that add further complexity and encourage multinational companies to keep their money abroad or defer paying U.S. taxes. Recognizing that not all businesses have foreign sourced income, reform should also work to ensure our tax system fairly promotes innovative and competitive practices across business tax structures.

**Principle 3: Revitalize domestic manufacturing.** Most Americans working in private enterprise do so for small or medium sized businesses – businesses that often do not have any operations outside of the United States. We need to ensure any comprehensive tax reform will help our domestic manufacturers grow and that international tax reform is not balanced on the backs of these U.S. job creators.

**Principle 4: Encourage innovation, high-tech manufacturing and entrepreneurialism.** Our tax system should create a foundation that proactively encourages American innovation. We should reform our system to nurture promising infant industries and help small business people and entrepreneurs to thrive and grow. Incentivizing research, development, manufacturing and commercialization of innovative work in the U.S. will create a growth environment that facilitates job creation and helps American businesses compete. Our tax system should accommodate new technologies and encourage growth by promoting investments in developing innovations and supporting start-up programs, manufacturing and small business investors. Tax reform should address the challenges of mobile capital by examining new tax structures to promote U.S. manufacturing, provide incentives to encourage domestic growth, and protect intangible goods and intellectual property.

**Principle 5: Recognize the international mobility of capital.** The fungibility of capital in today's economy creates a large incentive for multinational corporations to shift their income to the most favorable tax environment. One of the primary means of income shifting is through the differentiated treatment of "active" versus "passive" income across international lines. The definition of "active" income should be reformed to reflect the reality of modern business practices, such as the increasing role of the knowledge-based economy, our growing services sector, and intellectual property, as well as other activities that are directly related to growing the business. Tax reform should properly define the different types of income to discourage inappropriate income shifting and reflect the underlying economics of business transactions.

**Principle 6: Spur innovation and creativity through an educated workforce.** The American workforce is the lifeblood of the economy and the wellspring of innovation. To provide better opportunities for our workers to succeed, we must continue to invest in greater access to mid-career education and skills, and promote national excellence in science, technology, engineering and mathematics (STEM) education. The mobility of jobs and opportunities underscores the importance of providing education and skills training to those entering the workforce as well as those who need retraining. There are a myriad of tax benefits currently geared toward defraying the cost of education and incentivizing saving for future education. Unfortunately, the complexity of these various incentives make it difficult for the average American to determine which of the tax benefits may be the most effective due to income phase-outs and other restrictions. Tax reform must continue to prioritize educating both future and existing workers while simplifying the system to make it easier to understand.

**Principle 7: Encourage growth through responsible financing mechanisms.** Our tax system should help responsible businesses move forward on projects that allow them to grow, hire or finance large purchases, but it should be structured in a way that does not encourage excessive leveraging or steer them into a decision that is not financially responsible. Our current system directly impacts the behaviors of businesses and consequently, any attempt to alter these tax treatments should consider the behavioral impacts. Our tax system should strive to balance the desire for strong economic growth with efforts to promote job creation, long-term investments and de-leveraging.

**Principle 8: Restore transparency and trust in government.** Many Americans believe the current tax code is biased in favor of the wealthy and special interests while doing little to nothing to provide help to ordinary families struggling to get by. The tax system should not allow politically empowered interests to manipulate the law at the expense of ordinary citizens without those same means. Tax reform should strengthen public trust and confidence through a simpler and more transparent and equitable system. The rules should not unfairly discriminate against any one sector or industry, or against any individual or group of citizens. Rather, the tax system should be transparent and simple so that the public has confidence that the tax system is fair, effective, and that revenue collected is used for the public good.

**Principle 9: Build a predictable, stable tax system and process.** A stable and reliable tax system is crucial to long-term growth and investor confidence. Tax reform should create certainty in the tax code so businesses and individuals can effectively plan for the future. Tax reform should produce a more predictable system that is not subject to rapidly changing political pressures. Revisiting critical tax provisions for our economic growth on an annual basis, such as the R&D tax credit, produces a more inefficient tax code and creates an unpredictable environment. Reform should create predictability in the tax system to encourage sound investments and give individuals and businesses confidence in the government's decision making process.

**Principle 10: Establish effective transition rules.** When the government undertakes major changes to federal law, transition rules must be effectively written in order to allow sufficient time for individuals, businesses and taxing authorities to make the appropriate adjustments. As we reform our tax system, we should also transition to new technologies and tax filing systems that help taxpayers adapt to and comply with changes, as well as, assist authorities in overseeing a new system. Effective transition rules will avoid improperly burdening taxpayers and assist businesses with short and long-term tax planning.